GOVERNMENTAL COSTS
AND
TAX LEVELS

By

LEWIS H. KIMMEL
With the collaboration of
MILDRED MARONEY

WASHINGTON, D. C.
THE BROOKINGS INSTITUTION
1948

Set up and printed
Published March 1948

Printed in the United States of America
Cornelius Printing Company
Silver Spring, Maryland

PREFACE

Both major political parties in the United States are now committed to the principle that sound fiscal policies are essential for economic stability. While it is recognized that budget deficits may be expected in periods of depression—because of shrinking revenues and increasing expenditures for relief purposes and to stimulate recovery—it is nevertheless agreed that over a period of years receipts must equal expenditures; and, if debts incurred in periods of great emergency are to be reduced to manageable proportions, revenues must exceed expenditures.

Developments since the war have convinced many people that fears formerly held with respect to the ability of the United States government to maintain fiscal stability were grossly exaggerated. Despite the continuance of federal expenditures on a level far higher than had been contemplated, budget operations show a sizable surplus, and it is believed by many that substantial tax reductions may now be made and that at the same time some reductions in the national debt can be achieved. The view is widespread that this country has again demonstrated its capacity to meet the enormous financial requirements of depression and of war without undermining its financial foundations.

The purpose of this study is to subject this conception to realistic tests. To gauge the prospect for maintaining financial stability, it is necessary to view the problem in the perspective of something like a five-year period. Only in this way can one see the outcome of current expenditure trends and appraise the effects of possible fluctuations in the national income on fiscal stability and the possibility of tax reduction. Concretely, where will current commitments and policies with respect to such major classes of expenditures as veterans' benefits, social welfare and education, foreign aid and relief, and national defense lead us? What are the implications of these trends for tax reduction?

The method followed in the study is as follows: First, we seek, by a study of factors and forces affecting the level of expenditures, to indicate on a conservative basis what the level is likely to be some five years hence. Second, we make a detailed analysis of the revenues needed to cover such expenditures—assuming the continuance of a relatively high level of national income. Third, we consider the urgent demands for tax reductions in relation to the expenditure and revenue requirements that have been indicated. Fourth, we show how the situation with respect to revenues would be affected by even moderate reductions in the level of national income.

In contrast with most discussions of the fiscal situation, this study covers the states and their political subdivisions, in addition to the federal government. This is essential if we are to gauge the extent of the tax load that the American economy would have to carry.

This volume is in the nature of a sequel to a preliminary study by the same author entitled *Postwar Fiscal Requirements: Federal, State, and Local,* published in 1945. Dr. Kimmel wishes to record here his indebtedness to members of the Brookings Institution staff for many helpful suggestions and criticisms, and also to many individuals in government agencies and private organizations familiar with special phases of public finance. Mildred Maroney prepared the important section which projects forward the requirements for veterans' benefits. The co-operating committee has consisted of Harold W. Metz, Henry P. Seidemann, and myself.

HAROLD G. MOULTON,
President.

Washington
March 1948

CONTENTS

TABLES

THE BROOKINGS INSTITUTION

The Brookings Institution—Devoted to Public Service through Research and Training in the Social Sciences—was incorporated on December 8, 1927. Broadly stated, the Institution has two primary purposes: the first is to aid constructively in the development of sound national policies; and the second is to offer training of a supergraduate character to students of the social sciences.

The responsibility for the final determination of the Institution's policies and its program of work for the administration of its endowment is vested in a self-perpetuating board of trustees. It is the function of the trustees to make possible the conduct of scientific research under the most favorable conditions, and to safeguard the independence of the research staff in the pursuit of their studies and in the publication of the results of such studies. It is not a part of their function to determine, control, or influence the conduct of particular investigations or the conclusions reached, but only to approve the principal fields of investigation to which the available funds are to be allocated, and to satisfy themselves with reference to the intellectual competence and scientific integrity of the staff. Major responsibility for "formulating general policies and coordinating the activities of the Institution" is vested in the president. The by-laws provide also that "there shall be an advisory council selected by the president from among the scientific staff of the Institution."

Authors of studies published by the Institution have had the advice, criticism, and assistance both of an administrative officer and of a co-operating committee selected from the staff. In manuscript accepted for publication, the author has freedom to present his final interpretations and conclusions, although they may not necessarily be concurred in by some or all of those who co-operate with him or by other members of the staff. The Institution in publishing the work assumes the responsibility that it meets reasonable tests of scholarship and presents data and conclusions worthy of public consideration.

BOARD OF TRUSTEES

The study upon which this book is based was made possible by funds granted by The Maurice and Laura Falk Foundation of Pittsburgh. However, the Falk Foundation is not the author, publisher, or proprietor of this publication and is not to be understood as approving or disapproving by virtue of its grant any of the statements and views expressed herein.

CHAPTER I

THE TREND OF GOVERNMENTAL COSTS

The trend in the cost of government has long been sharply upward. Though this may seem a truism, there is abundant reason why the long-term upward trend should be stressed at this time. Major wars are inevitably followed by greatly increased *peacetime* costs. Expenditures for veterans' benefits and interest, among other objects, have been catapulted to levels which as recently as 1940 would have seemed incredible. While it is generally understood that costs such as these will be higher than before the war, the extent of the over-all increase in peacetime governmental costs has not been fully appreciated.

The primary purpose of this chapter is to summarize the estimates of prospective federal, state, and local cash expenditures for the fiscal year ending in 1952, which is assumed to be a reasonably settled postwar year—neither extreme boom nor substantial depression. The figures for 1952 are based on the analysis in Chapter II.[1] Comparative figures for 1940 and 1946 are included in the table on page 3 and the chart on page 4.

The estimates for 1952, it should be emphasized, are what we think governmental costs *will be,* not what they *should be.* Our sole object is to indicate, in the light of existing commitments and current trends, the probable level of expenditures in the years ahead. In preparing the estimates for the several functions on which this summary is based, every effort has been made to rule out individual judgments concerning the amounts government should spend. It should thus not be assumed that we regard the indicated level of expenditure as essential.

The amounts shown for 1952 have been determined following a careful examination of available evidence as to the probable level of governmental costs, together with factors influencing these costs. Major consideration has been given to public

[1] In the summary table the estimates for 1952 have been rounded to the nearest multiple of 50 millions.

policies—existing and emerging—affecting expenditures and expenditure trends. The growth of population, probable trends in production and national income, and possible changes in the price level have of course been taken into account.

Three general assumptions underlie the estimates:

1. That the cost-of-living and general price indexes will be about 50 per cent higher than in 1940, and that the compensation of governmental employees will be increased over 1940 by roughly the same proportion as the increase in the cost of living.

2. That the fiscal year 1952 will be one of generally satisfactory economic conditions, with substantially full employment.

3. That there will be no sharp change—as compared with 1940—in the distribution of total activities between the private and public sectors of the economy.[2]

Before referring to the figures, it should be emphasized that the estimates of governmental costs in this study are on a cash basis; our principal concern is with the amounts government will have to raise from the economy as a whole in order to cover its cash needs.[3] This basis contrasts sharply with that commonly used in compiling data for governmental expenditures, especially federal expenditures. "Expenditures" which take the form of transfers to trust funds are not here included.[4]

Duplications resulting from grants by one level of government to another have been eliminated in the summary table. When reference is made in this study to combined federal, state, and local expenditures, moneys transferred as grants have been counted only once. Grants have been uniformly regarded as expenditures of the first disbursing government.

[2] This implies that there will be no sharp change—as compared with 1940—in the ratio of the civilian employees of government to total civilian employees.

[3] The significance of the cash basis is discussed briefly in App. A. See p. 136.

[4] In the early 1950's federal budget expenditures (general and special accounts) will probably exceed cash expenditures, as here presented, by at least 3 billions to 4 billions a year. The difference is accounted for mainly by interest credits to trust and other funds and by tax refunds.

This procedure is essential if the requirements to be covered by each level of government from its own sources are to be accurately presented.

Federal cash expenditures for 1952 are estimated at slightly over 26 billions.[5] The range is placed at 23.4 billions to 31 billions. These totals do not include payments through the

FEDERAL, STATE, AND LOCAL CASH EXPENDITURES, ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940 AND 1946
(In millions of dollars)

Classification	1940	1946	1952		
			Minimum	Maximum	Probable
Federal	8,469	56,749	23,350	31,050	26,050
State	3,314	3,874	5,250	6,850	6,050
Local	5,633	6,287	7,950	8,900	8,400
Total	17,416	66,910	36,550	46,800	40,500
Social security payments[a]	642	1,765	2,250	2,750	2,500

[a] Not included in above totals.

social security trust funds, which are considered separately in this study; nor do they include any amounts for debt retirement. The indicated expenditure for 1952 is more than three times that for 1940. On the other hand, it is less than one half of federal expenditures for 1946.

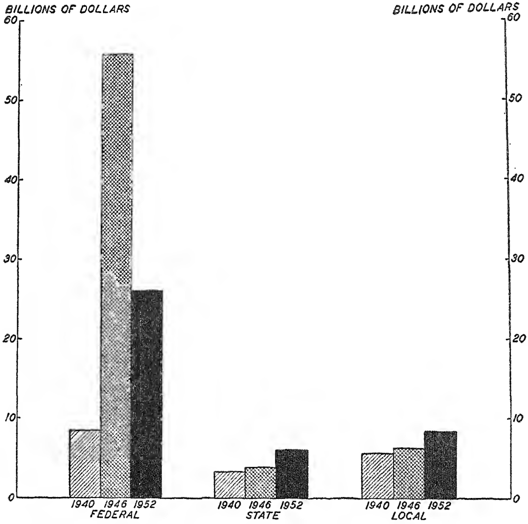
Probable state expenditures for 1952 are estimated at about 6.1 billions; the range is placed at roughly 5.2 billions to 6.8 billions. The indicated expenditures for 1952 are roughly 80 per cent larger than those for 1940 and about 55 per cent above the 1946 level. The totals shown in the table above are for expenditures financed by the states from their own sources. Gross functional expenditures, including those

[5] This figure is not comparable to recent estimates of federal expenditures. In addition to noncash items, the President's budget includes roughly 2 billions for tax refunds in each of the fiscal years 1948 and 1949. In the present study refunds are not counted as expenditures; all revenue estimates are net after refunds. Another factor is that the official budget totals have been increased to some extent by transfers between corporate accounts and general accounts.

financed from federal grants as well as grants to local governments, will amount to 8.1 billions in 1952, according to our estimates.

Local cash expenditures for 1952 are estimated at 8.4 billions, as compared with 5.6 billions for 1940 and 6.3 billions for 1946. Minimum and maximum estimates for 1952 are 7.9 billions and 8.9 billions. The total of 8.4 billions is for expenditures financed from local sources including local shares

Estimated Federal, State, and Local Cash Expenditures for the Fiscal Year 1952 Compared With 1940 and 1946



in state-administered taxes; expenditures covered from grants are excluded. The gross total, including expenditures financed from grants and a small amount of grants to other governments, is estimated at 11.2 billions.

State and local expenditures are often considered as a unit, especially when it is desired to compare the relative burden-

someness of federal expenditures and those of other governments. Our estimates indicate that in 1952 state and local expenditures financed from their own sources will amount to roughly 14.5 billions, or a little over 60 per cent more than in 1940 and 40 per cent above 1946. In 1952 state and local expenditures will be 55 per cent as large as those of the federal government, according to our estimates. In 1940, on the other hand, state and local cash expenditures were slightly larger than federal expenditures.

Combined cash expenditures of federal, state, and local governments are estimated at 40.5 billions for 1952. The minimum and maximum estimates are 36.5 billions and 46.8 billions. The estimate of 40.5 billions for 1952 is almost two and one half times expenditures for 1940.

Additional expenditures will be financed through the social security trust funds. The probable requirement, which is shown separately in the table on page 3, is estimated at about 2.5 billions for 1952. These payments are part of the obligations which government must meet. The entire amount for 1952 will be covered from special social security taxes, according to our estimates.[6] A more detailed discussion of social security finances will be found in Chapter VII.

It should be added that the estimates in this summary do not include any provision for debt retirement. At this juncture it is not certain whether a systematic program of debt reduction comparable to that followed after World War I will be adopted. It seems certain, however, that an effort will be made to reduce the federal debt in years when production and national income are at high levels. Any amounts specifically allocated for debt retirement would of course increase revenue requirements.[7]

[6] The excess of receipts is placed at about 2.3 billions in Chap. 7. Under our system of social security finance, no attempt is made to correlate revenues and cash requirements.

[7] In tables showing expenditures for a period of years, debt retirements should be excluded. Otherwise, the same amount is counted twice: (1) when the borrowed funds are spent; and (2) when the debt incurred is retired.

CHAPTER II

ESTIMATES OF EXPENDITURES BY FUNCTIONS

In this chapter we shall endeavor to estimate the probable magnitude of expenditures for the several governmental functions. Though the estimates are presented as for the fiscal year 1952, they should be regarded as for a typical or average year in the early 1950's.

In preparing estimates for a future year, the varying status of expenditures must be kept in mind. Some expenditures are contractual in nature. Interest on the public debt and obligations incurred under construction contracts are examples. Another segment of expenditures might be called quasi-contractual. Salaries of officials and employees fixed by statute are illustrations. For other objects of expenditure there are controlling laws which are tantamount to commitments. The laws governing veterans' benefits and state statutes providing grants to local units for school purposes are familiar examples. Though the statutes are subject to amendment and repeal, their net effect has been to increase the rigidity of public expenditures. That is to say, they tend to narrow the volume of expenditures subject to immediate control.

Authorizations for appropriations influence expenditures for a wide variety of purposes. Contrary to what is sometimes assumed, however, authorizations are not always followed by appropriations. In some instances they are definite as to both time and amount and have come to be regarded as more or less equivalent to specific commitments. Federal highway aids are an example. Other authorizations are definite as to amount but are approved without reference to a given year or years. The rivers and harbors and flood control authorizations are illustrations. A third class might be called determinable. Thus, the controlling factor in the federal grants to the states for aids to aged persons is the matching provision rather than the basic authorization. A fourth class of authorizations might be called general and indefinite. Grants

to the states for the control of tuberculosis and venereal diseases are examples.[1]

Certain other general policies established by law also exert a great influence on the volume of expenditures. While these policy commitments usually lack the definiteness of those mentioned above, and may vary appreciably from time to time, the policies are often regarded as more or less settled in character. The policy with respect to the maintenance of agricultural prices is an example. In addition, numerous long-established activities are regularly provided for by annual appropriations, without advance authorizations or commitments of any kind. Many of the operating expenses of executive departments are in this category.

With this brief statement of our approach to the problem, we turn to the estimates for the several functions. The estimates for the three levels of government are shown in the tables on pages 9 to 11 and the charts on pages 8 and 13. Combined federal, state, and local estimates will be found in the table on page 12.

I. NATIONAL DEFENSE

Expenditures for national defense are estimated at 9.5 billions for 1952. The range is placed at 8.8 billions to 10.5 billions. This function will account for more than one third of all federal expenditures and between one fourth and one fifth of combined federal, state, and local expenditures, according to our estimates.

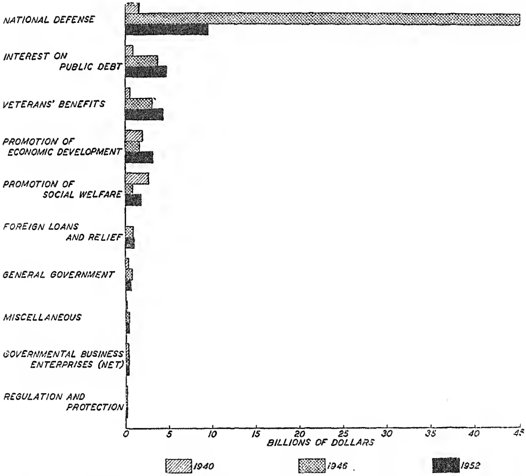
National defense policy. Our national defense policy in the years immediately ahead will be centered mainly on two commitments. First, there is the long-run commitment to provide for the defense of the United States. Second, there is the obligation to maintain in the occupied areas of Europe and the Far East the forces necessary for policing requirements.

[1] The amount authorized in these cases is "a sum sufficient to carry out the purposes of this subsection." 58 Stat. 693.

As long as occupation requirements continue, the defense establishment cannot be restored to a settled peacetime basis.

Defense policy is now being reoriented in the light of the lessons of World War II. Because of changes in the character of warfare, together with the relative weakness of our former Western European allies, a more or less complete reformulation of defense policy has become necessary. Though progress has been slow, the steps taken in the next few years will

ESTIMATED FEDERAL CASH EXPENDITURES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940 AND 1946



doubtless result in a defense establishment that will differ radically from that of a decade ago.

A defense policy for the future will necessarily assume that warfare will become increasingly mechanized. The great forward strides in mechanization during and since World War II, together with the development of guided missiles and the

Federal Cash Expenditures, Estimates for the Fiscal Year 1952
Compared With 1940 and 1946

(In millions of dollars)

Purpose of Expenditure	1940	1946	1952 Minimum	1952 Maximum	1952 Probable
NATIONAL DEFENSE	**1,546**	**44,950**	**8,750**	**10,500**	**9,500**
VETERANS' BENEFITS	**544**	**3,106**	**4,250**	**5,100**	**4,377**
REGULATION AND PROTECTION	**132**	**112**	**175**	**205**	**190**
Law enforcement and public safety	89	81	120	140	130
Regulation of commerce and industry	43	31	55	65	60
PROMOTION OF ECONOMIC DEVELOPMENT	**1,957**	**1,652**	**2,695**	**3,615**	**3,140**
Transportation	340	645	905	1,115	1,000
Commerce and industry	14	18	30	50	40
Labor interests	15	86	70	100	85
Agriculture	1,266	639	585	920	750
Other natural resources	322	264	1,105	1,430	1,265
PROMOTION OF SOCIAL WELFARE	**2,674**	**837**	**1,475**	**2,030**	**1,785**
Education	34	44	220	395	335
Public health and sanitation	38	161	180	225	200
Recreation	22	6	25	35	30
Public assistance	2,502	432	860	1,125	1,000
Social security administration	74	72	70	90	80
Housing	4	122	120	160	140
INTEREST ON PUBLIC DEBT	**882**	**3,717**	**4,400**	**5,060**	**4,730**
GENERAL GOVERNMENT	**339**	**791**	**610**	**725**	**665**
Legislative, judicial, executive	315	687	450	525	490
Foreign relations	24	104	160	200	175
FOREIGN LOANS AND RELIEF		**894**	**500**	**3,000**	**1,000**
MISCELLANEOUS	**95**	**385**	**300**	**400**	**350**
GOVERNMENTAL BUSINESS ENTERPRISES (net)	**300**	**305**	**200**	**400**	**300**
TOTAL	**8,469**	**56,749**	**23,355**	**31,035**	**26,037**

STATE CASH EXPENDITURES,
ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940 AND 1946

(In millions of dollars)

Purpose of Expenditure	1940[a]		1946[a]		1952								
					From Own Funds			From Grants			Total		
	From Own Funds	Total	From Own Funds	Total	Minimum	Maximum	Probable	Minimum	Maximum	Probable	Minimum	Maximum	Probable
VETERANS' BENEFITS	16	16	30	30	300	500	400				300	500	400
REGULATION AND PROTECTION	219	219	253	253	320	370	345				320	370	345
Law enforcement and public safety	154	154	178	178	220	250	235				220	250	235
Regulation of commerce and industry	65	65	75	75	100	120	110				100	120	110
PROMOTION OF ECONOMIC DEVELOPMENT	902	1,135	1,033	1,146	1,493	1,904	1,740	631	766	686	2,124	2,670	2,426
Transportation	822	1,021	902	971	1,345	1,710	1,570	540	645	580	1,885	2,355	2,150
Commerce and industry	4	4	6	6	8	12	10				8	12	10
Labor interests	3	6	2	2	5	12	10	50	70	60	55	82	70
Agriculture	53	78	73	110	80	90	85	35	45	40	115	135	125
Other natural resources	20	26	50	57	55	80	65	6	6	6	61	86	71
PROMOTION OF SOCIAL WELFARE	1,898	2,305	2,239	2,886	2,692	3,405	3,020	1,039	1,414	1,259	3,731	4,819	4,279
Education	963	990	1,279	1,327	1,597	1,925	1,740	185	355	295	1,782	2,280	2,035
Public health and sanitation	28	50	38	105	65	85	75	70	80	75	135	165	150
Recreation	12	12	17	17	20	40	30				20	40	30
Public assistance	895	1,195	890	1,359	980	1,290	1,125	730	905	825	1,710	2,195	1,950
Social security administration		58		63				54	74	64	54	74	64
Housing			15	15	30	65	50				30	65	50
INTEREST ON PUBLIC DEBT	121	121	73	73	130	170	145				130	170	145
GENERAL GOVERNMENT	168	168	205	205	280	330	305				280	330	305
MISCELLANEOUS	43	87	158	166	100	200	160	40	60	50	140	260	210
GOVERNMENTAL BUSINESS ENTERPRISES (net)	−53	−53	−117	−117	−70	−50	−60				−70	−50	−60
TOTAL	3,314	3,998	3,874	4,642	5,245	6,829	6,055	1,710	2,240	1,995	6,955	9,069	8,050

[a] The differences between the amounts shown in the two columns represent expenditures financed from grants.

LOCAL CASH EXPENDITURES,
ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940 AND 1946

(In millions of dollars)

Purpose of Expenditure	1940[a]		1946[a]		1952								
					From Own Funds			From Grants			Total		
	From Own Funds	Total	From Own Funds	Total	Minimum	Maximum	Probable	Minimum	Maximum	Probable	Minimum	Maximum	Probable
REGULATION AND PROTECTION	**638**	**646**	**805**	**815**	**980**	**1,130**	**1,055**	**10**	**20**	**15**	**990**	**1,150**	**1,070**
Law enforcement and public safety	611	619	765	775	940	1,080	1,010	10	20	15	950	1,100	1,025
Regulation of commerce and industry	27	27	40	40	40	50	45				40	50	45
PROMOTION OF ECONOMIC DEVELOPMENT	**751**	**972**	**835**	**1,182**	**1,075**	**1,315**	**1,195**	**506**	**657**	**587**	**1,581**	**1,972**	**1,782**
Transportation	682	902	750	1,097	995	1,205	1,100	505	655	585	1,500	1,860	1,685
Agriculture	43	43	55	55	50	70	60				50	70	60
Other natural resources	26	27	30	30	30	40	35	1	2	2	31	42	37
PROMOTION OF SOCIAL WELFARE	**2,694**	**3,829**	**3,091**	**4,380**	**4,120**	**4,530**	**4,315**	**1,851**	**2,381**	**2,131**	**5,971**	**6,911**	**6,446**
Education	1,577	2,286	2,001	2,915	2,625	2,790	2,705	1,350	1,725	1,550	3,975	4,515	4,255
Public health and sanitation	368	371	480	480	550	630	585	10	20	15	560	650	600
Recreation	170	170	200	200	235	285	260				235	285	260
Public assistance	579	1,001	400	774	670	765	715	490	635	565	1,160	1,400	1,280
Social security administration		1		1				1	1	1	1	1	1
Housing			10	10	40	60	50				40	60	50
INTEREST ON PUBLIC DEBT	**490**	**490**	**387**	**387**	**400**	**460**	**430**				**400**	**460**	**430**
GENERAL GOVERNMENT	**601**	**601**	**750**	**750**	**920**	**1,000**	**960**				**920**	**1,000**	**960**
MISCELLANEOUS	**414**	**461**	**364**	**473**	**400**	**425**	**410**	**50**	**85**	**70**	**450**	**510**	**480**
GOVERNMENTAL BUSINESS ENTERPRISES (net)	**45**	**45**	**55**	**55**	**50**	**70**	**60**				**50**	**70**	**60**
TOTAL	5,633	7,044	6,287	8,042	7,945	8,930	8,425	2,417	3,143	2,803	10,362	12,073	11,228

[a] The differences between the amounts shown in the two columns represent expenditures financed from grants.

Combined Federal, State, and Local Cash Expenditures, Estimates for the Fiscal Year 1952 Compared With 1940 and 1946

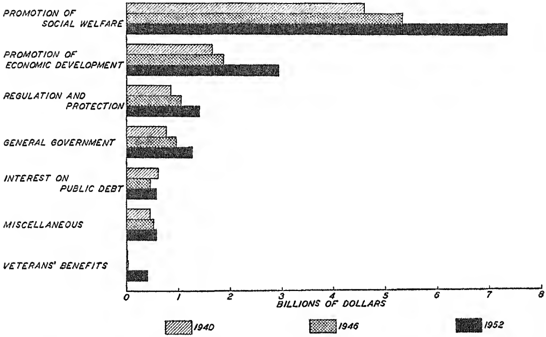
(In millions of dollars)

Purpose of Expenditure	1940	1946	1952 Minimum	1952 Maximum	1952 Probable
NATIONAL DEFENSE	**1,546**	**44,950**	**8,750**	**10,500**	**9,500**
VETERANS' BENEFITS	**560**	**3,136**	**4,550**	**5,600**	**4,777**
REGULATION AND PROTECTION	**989**	**1,170**	**1,475**	**1,705**	**1,590**
Law enforcement and public safety	854	1,024	1,280	1,470	1,375
Regulation of commerce and industry	135	146	195	235	215
PROMOTION OF ECONOMIC DEVELOPMENT	**3,610**	**3,520**	**5,263**	**6,834**	**6,075**
Transportation	1,844	2,297	3,245	4,030	3,670
Commerce and industry	18	24	38	62	50
Labor interests	18	88	75	112	95
Agriculture	1,362	767	715	1,080	895
Other natural resources	368	344	1,190	1,550	1,365
PROMOTION OF SOCIAL WELFARE	**7,266**	**6,167**	**8,287**	**9,965**	**9,120**
Education	2,574	3,324	4,442	5,110	4,780
Public health and sanitation	434	679	795	940	860
Recreation	204	223	280	360	320
Public assistance	3,976	1,722	2,510	3,180	2,840
Social security administration	74	72	70	90	80
Housing	4	147	190	285	240
INTEREST ON PUBLIC DEBT	**1,493**	**4,177**	**4,930**	**5,690**	**5,305**
GENERAL GOVERNMENT	**1,108**	**1,746**	**1,810**	**2,055**	**1,930**
Legislative, judicial, executive	1,084	1,642	1,650	1,855	1,755
Foreign relations	24	104	160	200	175
FOREIGN LOANS AND RELIEF		**894**	**500**	**3,000**	**1,000**
MISCELLANEOUS	**552**	**907**	**800**	**1,025**	**920**
GOVERNMENTAL BUSINESS ENTERPRISES (net)	**292**	**243**	**180**	**420**	**300**
TOTAL	**17,416**	**66,910**	**36,545**	**46,794**	**40,517**

atomic bomb, have meant a virtual revolution in the character of warfare. Progress has been so rapid that our thinking has not yet become adjusted to the implications of a war in which atomic bombs and pilotless weapons, among other innovations, would play dominant roles.

Among the lessons of World War II, the fact that air power will doubtless play a leading role for an indefinite period is in some respects the most significant. Plans of the military authorities call for an air force comprising a large portion of total army and navy personnel. Acquisition of planes is a major item in current procurement programs and will perhaps be of even greater relative importance in the near future.

Estimated State and Local Cash Expenditures for the Fiscal Year 1952 Compared With 1940 and 1946[a]



[a] Governmental business enterprises are not included in this chart. See tables on p. 10 and p. 11.

Another lesson of World War II is that unified air, land, and sea operations are indispensable in modern warfare. A unified defense establishment is now in the process of being organized. In the long run, unification of the services should mean both more efficient and more economical operation of the defense establishment. Pending the substantial completion of unification, however, these advantages will be largely unrealized.

It should be added that there will undoubtedly be a tendency to continue substantial expenditures for obsolescent military methods. The powerful influence of military tradition will inevitably mean a lag in the adjustment to changed conditions. In the estimates that follow this lag has been taken into account.

One of the few certainties in national defense is that our policy will provide for only a moderate-sized standing army. Present plans call for a small standing or regular army, which could be quickly re-enforced in an emergency by adequately trained citizen reserves. A defense program based on the availability of large numbers of trained reserves is regarded by the military authorities as preferable to one relying solely on the regular armed services and embracing a larger regular army personnel. However, a highly important policy decision has not yet been made. At this time we do not know whether, in an emergency, reliance for expanded personnel would be placed mainly upon men who have completed a compulsory training program.

Estimates of expenditures. Because of the many uncertainties, our estimate of 9.5 billions for defense expenditures is necessarily a very rough approximation. This figure is based on estimated service personnel—officers and men—of 1,400,000, in the absence of a compulsory military training program. Of this total, approximately 925,000 would be in the Army and 475,000 in the Navy, including the Marine Corps.[2] The combined requirement for pay, subsistence, travel, training, clothing, welfare, and medical care has been placed at $3,000 per man. The estimate for 1.4 million men thus becomes 4.2 billions.[3]

Costs directly related to personnel will be strongly influenced by the proportion of total personnel deployed overseas. Though there is a possibility that in 1952 a smaller proportion

[2] The budget estimates for the fiscal year 1949 assume an average military strength of 1,423,000 officers and enlisted personnel, or "about the same as the current strength of the armed forces." *The Budget of the United States Government for the Fiscal year ending June 30, 1949,* p. M 15.

[3] Further details will be found in App. B. See p. 140.

of total personnel will be deployed overseas than at present, this is by no means certain.[4] Current plans are based on the assumption that occupational requirements will continue more or less indefinitely. In this connection, it is significant that costs may soon be increased because of the necessity to assume responsibilities hitherto carried by Great Britain. Another factor affecting costs per man is the gradual ascendancy of the Air Force. Because of the large proportion of technicians, ratings are generally higher than in other services. The higher ratings in turn are reflected in the average rates of compensation.

For all other military purposes we estimate that over 5 billions will be expended in 1952. This figure, which embraces procurement, research and development, construction, operation and maintenance, and citizen-reserve activities, is somewhat lower than projected expenditures for the fiscal year 1949. However, it is not assumed that all categories of expenditures will decline. On the contrary, we believe that some objects of expenditure such as research and development will show a fairly pronouncd upward trend, especially after unification and the reorientation of policy referred to previously have been substantially completed.

We next consider how the above estimates might be affected by a compulsory training program. The first point to be emphasized is that such a program would represent an alternative approach to national defense. For this reason there would be little justification for regarding expenditures for the training program as solely in the nature of an extra cost. For the first year or two total defense expenditures would almost certainly be larger, but in later years this would not necessarily be the case.

At the outset two opposing trends would doubtless develop.

[4] At the beginning of the calendar year 1947 roughly one half of total army personnel were stationed outside the United States; a substantial portion of overseas personnel—but by no means all—were stationed in occupied areas.

There would be an immediate need for a large and competent instructional staff, which would tend to cause a rise in personnel. Though most of this staff might be drawn from existing personnel, some additions and replacements would be necessary. A temporary increase in total regular personnel would no doubt ensue.

On the other hand, an opposite trend would probably set in almost as soon as the program was adopted. If substantial appropriations for the training program should be approved, other defense appropriations would be virtually certain to be reduced. Though expenditures not classed as personnel costs would no doubt be affected to some extent, a substantial portion of any offsetting saving would probably come from a reduction in regular personnel. Following the period of readjustment, regular personnel might be 100,000 to 200,000 lower than it would be if the proposed program were not adopted.

Since both the adoption and form of the universal training program are uncertain, we shall not attempt to estimate precisely its effect on defense costs for 1952. The estimate of 1,750 millions for the program envisaged by the President's Advisory Commission[5] suggests that the initial impact would probably be substantial. But, as explained above, forces would immediately set in which would tend to bring about lower expenditures for other defense activities. By the third or fourth year the specific costs of the training program might be largely absorbed.

Regardless of the approach, national defense costs for the next five years are certain to be strongly influenced by the aftermath of war. Though our estimates assume only moderate reductions from present costs, this does not mean that we believe defense expenditures will remain indefinitely at the high level indicated. Our longer-run defense requirements will be determined by a variety of factors, most of them in-

[5] *A Program for National Security,* Report of the President's Advisory Commission on Military Training, May 29, 1947, p. 36.

ternational in character. While it is easy to visualize a situation that would permit the reduction of defense expenditures by the middle or late 1950's to roughly one half of the estimate for 1952, any such reduction would be possible only if plans for collective security are successful. Recent trends suggest that there is small likelihood of a marked downward readjustment in defense costs in the near future; there might even be an increase.

II. VETERANS' BENEFITS

Veterans' benefits are estimated at 4.8 billions for 1952, or roughly 12 per cent of all cash expenditures. Federal ex-

ESTIMATED FEDERAL EXPENDITURES FOR VETERANS' BENEFITS, FISCAL YEAR 1952
(In millions of dollars)

Classification	Probable Expenditures
Readjustment benefits:	
Education and training [a]	1,275
Guaranty of loans	64
Total, readjustment benefits	1,339
Pensions and compensation:	
World War II:	
Disability compensation [b]	1,142
Pensions, living veterans	12
Death pensions	251
Retirement pay of reserve officers	80
Total, World War II	1,485
Other wars [c]	750
Total, pensions and compensation	2,235
Other benefits:	
Hospital and medical services	610
Burial expenses	13
Administrative expenses [d]	180
Total, other benefits	803
Grand total	4,377

[a] Includes trainees under Public Law 346, 78 Cong. 2 sess. (58 Stat. 287), as amended, and Public Law 16, 78 Cong. 1 sess. (57 Stat. 43), as amended.
[b] Does not include extra subsistence of trainees under 57 Stat. 43.
[c] Includes regular establishment.
[d] Includes administration of the insurance system; does not include administration of the medical program.

penditures are estimated at 4.4 billions, and those of the states at 400 millions. A breakdown of the federal estimate is shown in the table on page 17.

Two assumptions underlie the federal estimates. First, with one exception it is assumed that benefits will be paid in accordance with the provisions of existing laws.[6] Second, although most of the authorized hospital expansion is still in the design stage, we shall assume that it will be completed before 1952 as provided by current plans.

Despite the uncertainties which necessitate these assumptions, the general trend of expenditures is fairly clear. It now seems certain that by 1952 the aggregate expenditures will be declining. This prospect is attributable to the fact that readjustment benefits, which are now so prominent, will be in various stages of termination.[7] In the long run, the trend of expenditures for benefits which are available permanently will overcome the effect of expiring benefits. In the early 1950's, however, the upward trend in pensions and compensation, and also in hospital and medical services, will be gradual.

Readjustment benefits. Expenditures for readjustment benefits are estimated at roughly 1.3 billions. Education and training benefits will account for over 95 per cent of the total. The veterans' loan program will still be in operation in 1952, but unemployment benefits will have terminated for all but a few thousand veterans.[8] The educational program will begin to terminate in 1956.

Education and training benefits are estimated at 1,275 millions for 1952. This estimate is based on an average enroll-

[6] We have recognized the probability that Congress will approve increases in provisions for education and training other than those authorized by Public Law 411, 80 Cong. 2 sess., approved Feb. 14, 1948.

[7] As these temporary benefits decrease, related administrative expenses should also decline.

[8] For veterans who were discharged prior to July 25, 1947, benefits for unemployment will terminate on July 25, 1949. (See Public Law 346, sec. 700(a), 78 Cong. 2 sess. and Public Law 239, 80 Cong. 1 sess., sec. 3.) However, veterans who enlisted under the Armed Forces Voluntary Recruitment Act of 1945 (59 Stat. 538) will retain entitlement for a longer period. In some cases entitlement will continue until July 25, 1952, but by that time expenditures will be negligible.

ment of about 850,000 veterans for 1951–52. With 2.8 million veterans enrolled at the present time, the training load has either attained or is nearing the peak.[9] Heavy veteran enrollments are expected to continue through 1950 or 1951. By 1952, however, the period of entitlement will in many cases have been exhausted.[10]

The average annual cost for each veteran is estimated at $1,500; the comparable average is now about $1,200.[11] We have used the higher figure for several reasons. First, although increases in subsistence allowances of full-time veteran students in educational institutions have already been approved, they are not yet reflected in expenditures. Second, although these increases do not affect provisions for veterans in on-the-job training, pending legislation will raise the limits on the total for subsistence and earned income. Third, the cost of tuition, supplies, and equipment has been increasing.

Our estimate of 64 millions for expenditures under the loan program is based on the assumption that 500,000 loans might be approved in 1952.[12] Approval of 500,000 loans would involve an expenditure of about 50 millions, representing payments to lenders equal to 4 per cent of the guaranteed portion which currently averages $2,500 per loan. In addition, there will be losses on the principal of outstanding loans. However,

[9] This figure includes disabled veterans who are training under the Vocational Rehabilitation Act. 57 Stat. 43.

[10] Although educational benefits will remain available until July 25, 1956, and in some cases until 1961, veterans who were discharged prior to July 25, 1947 must enter training before July 25, 1951. The maximum duration of training is 4 years, but this maximum is limited to veterans who served at least 3 years less 90 days, and to disabled veterans.

[11] There are many variables in this unit of cost. It depends on the proportion of part-time enrollments, for which basic allowances are prorated, and on the distribution of beneficiaries by marital and dependency status. It is also affected by the distribution of enrollments between two basic legislative authorizations. Although the option of vocational rehabilitation is limited to disabled veterans, it has entailed higher units of expenditure than those which are governed by provisions for education available to all veterans.

[12] At the end of the fiscal year 1947 nearly one million loans had been approved; and it is expected that this total will have increased to 1.6 millions by the end of 1948. While this figure represents only 10 per cent of the number of existing and potential veterans who are theoretically eligible, a declining proportion of applicants will constitute acceptable risks.

since 88 per cent of all the loans are for the financing of homes, we have assumed that most of them are sound.[13]

Pensions and compensation. Expenditures for pensions and compensation are estimated at 2.2 billions for 1952. Although the trend in these expenditures will then be upward, our estimate for 1952 is about equal to the present rate of expenditure. This apparent contradiction is explained by changes in the intervening period.

During the next two years, compensation for service-connected disabilities should be declining somewhat from the current level of expenditures. It is believed that the physical or mental conditions which justify this type of benefit have in many cases either improved or disappeared. Assuming a thorough review of cases, these changes would permit termination or reduction of the benefit. However, following such adjustment the trend will again be upward, because of the incidence of chronic disease.[14] Our estimate for disability compensation of World War II veterans is based on 1.7 million active cases in 1952.

The average payment per case is estimated at $56 a month, a substantial increase over the recent average of $42. The reason for this sharp rise is that the rating schedule was liberalized in 1945; as a result, the average degree of disability may be expected to rise from about 33 per cent to at least 40 per cent.[15] The cost for World War II veterans thus becomes 1,142 millions.

Payments other than disability compensation relating to World War II include pensions for nonservice-connected disability (total and permanent), retirement pay of reserve officers

[13] The major risk for the immediate future attaches to business loans, which account for 9 per cent of all the loans approved. Business loans may run for only 10 years, as compared with 25 years for home loans and 40 years for farm loans.

[14] This statement of factors underlying the trend applies especially to World War II veterans. In the case of World War I veterans, compensation has been declining since 1941 as a result of mortality.

[15] Compensation for disability rated at 40 per cent is now $55.20 per month. In addition, statutory compensation must be taken into account, but this does not affect the averages materially.

of the Army, and pensions to the dependents of deceased veterans. These are estimated at 12 millions, 80 millions, and 251 millions, respectively. Although payments for nonservice-connected disabilities will in the long run rise to a much higher level, they will not be an important component of expenditures in 1952, when World War II veterans will still be comparatively young. Expenditures for retirement of reserve officers are influenced by the fact that they are pensioned at a much higher rate than enlisted men.[16] Payments to survivors are mainly confined to service-connected deaths, but an increase in number can be expected.

Pensions and compensation for all groups other than veterans of World War II are estimated at 750 millions, compared with an expenditure of 429 millions in 1940. The difference is accounted for in part by a rise in the number of World War I cases and in part by increases in rates of payment. The trend in the number of beneficiaries is attributable to the rising mortality of World War I veterans, together with the fact that their survivors have recently obtained a legislative status similar to that of predecessor groups. It is also influenced by the incidence of nonservice-connected disability among aging veterans. The increase in rates of payment amounts to 38 per cent over those current in 1940.[17] Beneficiaries of the War with Spain and the Civil War have reeived comparable increases.

Other benefits. The benefits remaining to be discussed consist mainly of medical care and administrative expenses. These expenditures are estimated at 610 millions and 180 millions, respectively. Burial expenses, which are estimated at 13 millions, are the only other component.

The cost of medical care includes both the construction and

[16] Retirement pay of reserve officers is determined in the same manner as that of regular army officers. In other words, the amount is determined by base pay in service, three fourths of which is continued automatically on certification of retirement for disability by the Army. For enlisted men the degree of disability is the determining factor.

[17] This figure is the result of two separate increases of 15 per cent and 20 per cent.

operation of facilities. The construction program involves current and future expenditures of about 1.2 billions.[18] Though this program is behind original time schedules, the plans as revised call for completion in 1951. Accordingly, we have not included any allowance for construction in our 1952 estimate.[19]

The cost of operating hospitals will of course increase as construction is completed. The waiting list of patients, together with the incidence of illnesses which are not connected with military service, suggests that for a long period ahead applications for admission will absorb whatever capacity becomes available. At present the average daily bed occupancy in facilities operated by the Veterans' Administration is about 92,000 patients; in addition, 13,000 patients are cared for under contracts with other hospitals. For 1952 we have estimated costs on the basis of an average daily bed occupancy of 139,000, of which 123,000 might be cared for in veteran hospitals and 16,000 by contract hospitalization. (We assume that temporary hospitals which are now in operation will have been closed.) We have estimated operating costs at $8 per patient-day for veteran hospitals and $10 for patients in other hospitals; both figures are lower than current rates of expenditure. In addition, domiciliary care must be provided for about 20,000 veterans at approximately $2 a day. On this basis, the combined operating cost of these services would be 430 millions.

The latter estimate does not include out-patient treatment and examinations, and we have added 100 millions for this

[18] At the end of the fiscal year 1947, the unexpended balance of construction funds was 387 millions. In addition, the Veterans' Administration has been authorized to obligate 779 millions for further expenditure; these authorizations must be obligated before July 1, 1949.

[19] There is a possibility that more expenditures will be authorized; in view of rising costs, it is probable that additional funds will be needed to complete all the hospitals that are now in the design stage. However, we assume such additional expenditures would be made within the scheduled period of construction. The authorization of further expansion is logically precluded by the fact that the goal already envisaged represents the practical limit of facilities that can be staffed and operated.

purpose.[20] Other expenses for medical care include administration, operation of supply depots, and purchases of initial equipment for new hospitals. These items may be expected to bring the total cost of medical and hospital services to about 610 millions.

All other administrative expenses are estimated at 180 millions for 1952. Except in the case of insurance, these expenses should be roughly proportionate to the volume of expenditures to which they relate. Readjustment benefits, pensions, compensation, and burial benefits take the form of monetary disbursements which are made either directly to the beneficiaries or indirectly through colleges or loan agencies. The current ratio for administration of these items is about 5.5 per cent, as compared with less than 4 per cent before the war. Though the ratio should probably not exceed the latter figure, our estimate assumes a ratio of 4.5 per cent. Thus, the indicated expenditures for 1952 become 162 millions. Administration of the insurance system is estimated at 18 millions.[21]

The estimate of 4.4 billions for veterans' benefits is probably somewhere near the minimum that might be expected. Additions to coverage and higher rates would mean increased expenditures. In the past changes in basic laws have rarely resulted in reductions in costs; the main historical trend has been one of increasing liberality. Various proposals that would result in increased expenditures are now pending. Of these, the most important are: (1) pensions for World War I veterans on a basis of entitlement comparable to that of veterans of the Civil War and the War with Spain; and (2) for World

[20] The allocation for out-patient expenses is now estimated at about 120 millions. However, some reduction both in unit costs and the number of examinations should be possible as claims decrease and as an increasing proportion of treatments are handled in government clinics.

[21] This figure is considerably less than the current expenditures, which are affected by arrears in the records. On the other hand, it is about 10 times the cost of administering the insurance system in 1940.

War II veterans, the authorization of adjusted compensation comparable to the World War I "bonus."[22]

State benefits. State veterans' benefits are estimated at 400 millions for 1952. The minimum and maximum estimates are 300 millions and 500 millions.

State veterans' bonuses are estimated at 300 millions for 1952. This figure is based on a cumulative total of 3 billions for all the states which have authorized or will probably authorize payment of bonuses to World War II veterans.[23] It is here assumed that one tenth of this amount represents a cost properly allocable to 1952. No attempt has been made to forecast the exact schedule of expenditures.

Aids other than bonuses by the states are estimated at 100 millions. Every state has some type of veterans' program administered by a department, office, or agency.[24] These programs provide for several types of benefit which vary considerably among the states; they include educational scholarships, rehabilitation aids, medical care, housing aids, counseling services, and loan guaranties.[25] A number of other benefits, which do not affect expenditures directly, have also been provided by the states. Exemptions of specified amounts of assessed valuation and job preferences are examples.

III. REGULATION AND PROTECTION

Expenditures for regulation and protection are estimated at about 1.6 billions for 1952, or roughly 4 per cent of func-

[22] Although these are not the only proposals now pending, they are the most important both from the fiscal standpoint and from the standpoint of policy. They may develop into public issues at any time during the next ten years. In the case of World War II veterans, the question of a wider basis of entitlement to pensions will become an issue at a much later date.

[23] The total state debt authorized through March 1947 for veterans' bonuses aggregated 1.4 billions. In addition, bond issues under consideration by state legislatures totaled 2.2 billions; some of these may be scaled down or classed as doubtful.

[24] Council of State Governments, *Postwar State Taxation and Finance,* April 1947, p. 4, and Frank Bane, "State Fiscal Policy in Transition," National Tax Association, *Proceedings* (1946), p. 47.

[25] For convenient summaries of state veterans legislation, see Council of State Governments, *State Veterans Legislation Enacted During 1946,* October 1946, and "Action by the Legislators—1947", *State Government,* Vol. 20, pp. 190, 278.

tional expenditures. The comparable proportion for 1940 was 5.7 per cent.

Federal. Expenditures of the federal government under this heading are estimated at 190 millions. Law enforcement and public safety accounts for the bulk of the total—130 millions. Included are the intelligence and investigatory work of the Federal Bureau of Investigation, immigration and naturalization, the custody and care of prisoners, and overhead administration of the Department of Justice. Expenditures for the regulation of commerce and industry are estimated at 60 millions. Activities in this classification include the work of the Securities and Exchange Commission, the meat inspection unit of the Bureau of Animal Industry, the Interstate Commerce Commission, and the Federal Communications Commission.

State. State expenditures for regulation and protection are estimated at 345 millions. Of this amount, 235 millions would be spent for law enforcement and public safety, principally for penal and correctional institutions. Regulation of commerce and industry will require an estimated 110 millions. Activities in this category include supervision of financial institutions, insurance companies, public service corporations, and certain professions, together with the regulation of working conditions.

Local. Expenditures of local governments for regulation and protection are estimated at 1,070 millions, of which 15 millions would be covered by grants. These expenditures are accounted for mainly by police and fire departments. The estimated increase of roughly 400 millions over 1940 is mainly a result of higher pay-roll costs. Salaries and wages of these departments showed an upward trend during the war years, and this trend has been accentuated since the end of hostilities.[26] Local expenditures for the regulation of commerce and industry are of only minor importance.

[26] From 1940 to 1946 the salaries and wages of the fire departments of eighteen cities with populations of 200,000 to 500,000 (Jersey City excluded) rose from 24 millions to 32.1 millions—an increase of one third. *Municipal Year Book* (1941), p. 409, and (1947), pp. 349–50. In the same period the salaries and wages of the police departments of the same eighteen cities rose from 24.7 millions to 33.6 millions or by 36 per cent. The same (1941), p. 452 and (1947), pp. 388–89.

IV. PROMOTION OF ECONOMIC DEVELOPMENT

Expenditures for promotion of economic development are estimated at slightly over 6 billions for 1952, or about one seventh of the total for all functions. The 1940 proportion was approximately one fifth. The federal government will spend roughly 3.1 billions, according to our estimates. The comparable figure for the states is 1.7 billions, and that for local governments is 1.2 billions.[27]

Economic development embraces a wide range of activities. It includes the maintenance and development of highways, operation of airways, aids to aviation, and aids to other forms of transportation. It also includes expenditures in behalf of specific economic groups such as agriculture, business, and labor. Another category of expenditures is natural resources development exclusive of agriculture: flood control, public power projects, reclamation, and the new atomic energy program are the most important activities.

A large portion of expenditures for economic development is normally accounted for by capital outlays. The proportion for 1952 will probably be close to one half; if aids to agriculture are excluded it would be substantially higher. It is assumed that by 1952 shortages of materials, equipment, and man power, together with other difficulties retarding construction, will be less important than in 1946 and 1947. However, the possibility that they will still be a retarding factor in some cases is recognized.

Transportation

Combined federal, state, and local expenditures for transportation are estimated at about 3.7 billions for 1952. The range is placed at 3.2 billions to 4 billions. A breakdown of the combined estimate by objects of expenditure is shown in the table on page 27.

Federal. From the standpoint of amounts involved, highway grants to state and local governments are the most important

[27] It will be understood that the state and local estimates are exclusive of expenditures covered from grants.

class of federal expenditure for transportation. These grants are estimated at 500 millions for 1952, the annual amount provided by the Federal-Aid Highway Act of 1944.[28] Though this act established the level of grants only for the first three postwar years, it will probably set the pattern for a longer period.

FEDERAL, STATE, AND LOCAL EXPENDITURES FOR TRANSPORTATION, ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940

(In millions of dollars)

Classification	1940	1952 Minimum	1952 Maximum	1952 Probable
Federal:				
Highway grants	163	475	550	500
Other land transportation	6	30	40	35
Aids to aviation	31	200	250	230
Aids to navigation	36	120	150	135
Rivers and harbors	104	80	125	100
Federal total	340	905	1,115	1,000
State:				
State highways	777	1,300	1,600	1,475
Highway grants to local units	220	425	525	475
Aids to aviation		125	175	155
Waterways	4	5	15	10
Supervision and all other	20	30	40	35
State total	1,021	1,885	2,355	2,150
Less federal and local grants	199	540	645	580
State total, own funds	822	1,345	1,710	1,570
Local:				
Highways and streets	902	1,350	1,650	1,500
Aids to aviation		150	210	185
Local total	902	1,500	1,860	1,685
Less grants	220	505	655	585
Local total, own funds	682	995	1,205	1,100
Total: all governments	1,844	3,245	4,030	3,670

Thus far expenditures on account of grants under the 1944 act have been running well below 500 millions a year. Shortages of materials and labor, contracting difficulties, and high costs, among other problems, have caused a considerable lag

[28] 58 Stat. 838.

in the federal-aid highway program.[29] As a consequence, there is a possibility that annual payments to the states might exceed 500 millions for one or two years. Judging from present indications, however, the lag referred to will probably not soon be offset by a greatly accentuated boom. For an indefinite period, materials, labor, and equipment will be the limiting factors.

Because of the marked change in conditions since 1944, the assumption that later highway authorization acts will continue grants at 500 millions a year might be questioned. With the federal-aid construction program in full swing and costs well above those which seemed likely when the 1944 law was enacted, a case will doubtless be made for even higher grants. On the other hand, there is reason to believe strong pressures will continue to be exerted in favor of controlling total federal expenditures. In the absence of any indication to the contrary, the best assumption would seem to be that the prevailing figure will be continued.

Federal expenditures for the promotion of aviation are estimated at 230 millions for 1952. Two categories of expenditure account for the bulk of the total: (1) salaries and expenses of the Civil Aeronautics Administration; and (2) grants under the Federal Airport Act of 1946.[30] Salaries and expenses of the Civil Aeronautics Administration include the operating expenses of the nation's airways. The annual expenditure is now about 75 millions; our estimate for 1952 is 90 millions. Grants for airport construction are estimated at 75 millions; a gradual increase over a period of years seems likely. The balance of the estimate for aviation is accounted

[29] Thus, as of September 1, 1947, the active program of highway projects financed from federal-aid funds, for which plans were approved but construction not completed, involved a total estimated cost of 1,024 millions, of which the federal share was 519 millions. Of the latter amount, 423 millions consisted of funds authorized by the Federal-Aid Highway Act of 1944. As of September 1, 1947, completed projects financed from funds authorized by the 1944 act involved a total cost of 179 millions, of which the federal share was 93 millions. Letter from Public Roads Administration, Oct. 9, 1947.

[30] 60 Stat. 170.

for by the provision of air navigation facilities (15 millions) and the salaries and expenses of the National Advisory Committee for Aeronautics (50 millions).

The federal estimate for aviation does not include any amount for grants to the aviation industry. It has been widely proposed that, in view of the great importance of aviation for the future defense of the nation, federal grants should be made for developmental and research purposes. Though this type of grant has not been taken into account, this should not be construed as indicating that we believe the proposal may not be favorably considered. Our principal reason is that at this time there is no basis for gauging the magnitude of any expenditure that might be approved.

Navigation aids and facilities are estimated at 135 millions for 1952. Expenditures of the Coast Guard are estimated at 75 millions, a figure well below the current level of expenditures. Expenditures of the Maritime Commission are estimated at 60 millions.

Rivers and harbors expenditures are estimated at 100 millions for 1952. This figure represents a moderate decrease from the current level, as indicated by appropriations and estimates of expenditures for 1948. Current trends suggest that for some time flood control will take precedence over rivers and harbors (navigation) as an object of expenditure. Moreover, there are indications that water transportation may gradually become relatively less significant as an object of public works expenditure.

State. Expenditures on state highway systems are estimated at 1,475 millions for 1952. This figure includes federal moneys spent on state highways. The 1952 estimate is almost 90 per cent larger than expenditures for 1940.

State highway expenditures will for some years be strongly influenced by three factors making for larger expenditures: (1) the higher level of federal grants referred to above; (2) the sharp contraction in new construction during the war years; and (3) the substantial accumulated balances in state highway

funds. On the other hand, shortages of materials, equipment, and labor, together with other factors making for delay, will tend to restrict the volume of work on state highway systems. After these shortages are overcome our estimate of annual expenditures might prove to be conservative. At present, however, not even a rough forecast of the time when more favorable conditions will obtain is possible.

Highway grants to local governments are estimated at 475 millions. This figure includes certain federal moneys made available for local highway purposes. It is assumed that the policy initiated under the Federal-Aid Highway Act of 1944 will be continued.[31]

State expenditures for aids to aviation are estimated at 155 millions. Excluding 75 millions of federal moneys transferred for local airport construction, the estimated expenditure is 80 millions. Of the latter amount, perhaps 35 millions would also be paid to local governments as grants-in-aid.

Local. Expenditures of local governments for highways and streets are estimated at 1.5 billions for 1952. Of this total, 475 millions would be covered by federal and state moneys, leaving 1,025 millions to be financed from local funds. City and village highways and streets and rural roads not embraced within state highway systems account for almost the entire expenditure.

Local aids to aviation are estimated at 185 millions, of which 110 millions would be financed with federal and state funds. Construction and improvement of airports will account for the bulk of the expenditure.

Commerce and Industry

Expenditures for the promotion of commerce and industry are estimated at 50 millions for 1952. Of this amount, the federal government would spend 40 millions and the states 10 millions.

Federal activities classed under this heading include the

[31] This act allocated 125 millions a year for three years for projects on the federal-aid highway system in urban areas. 58 Stat. 840.

promotion of foreign and domestic trade, the protection of proprietary rights, and miscellaneous activities of the Department of Commerce. State activities comprise mainly the work of agencies and offices engaged in advertising the resources of the states. Local governments also spend small amounts for this purpose, but there is no adequate basis for a separate estimate.

Labor Interests

Expenditures for labor interests are estimated at 95 millions for 1952. Federal expenditures are placed at 85 millions and state expenditures from their own funds at 10 millions.

The larger part of the federal requirement is for the support of public employment offices. As presently constituted, this system comprises "the co-ordinated employment office facilities of the several states," but it is financed mainly by the federal government.[32] Grants for 1952 are estimated at 60 millions; appropriations for 1948 are 57 millions.

All other federal expenditures for labor interests are estimated at 25 millions. Included are the expenses of the National Labor Relations Board, the Federal Mediation and Conciliation Service, the Bureau of Labor Statistics, and overhead administration of the Department of Labor. The state estimate covers comparable expenditures by the states in behalf of labor.

Agriculture

Expenditures for agricultural purposes in 1952 are estimated at from 700 million to 1.1 billion dollars. All but a minor part of the total is accounted for by the federal government.

Federal. Expenditures of the federal government for agriculture amounted to roughly 1.3 billion dollars in 1940 and about 650 millions in 1946, as indicated in the table on page 9. In order to have some basis for estimating expenditures

[32] The provision of the Wagner-Peyser Act of 1935, 48 Stat. 113, requiring the states to provide matching funds has been waived only until July 1, 1949. We here assume that the matching provision will continue to be waived.

in 1952, it is first necessary to appraise the probable general position of agriculture in the light of recent and current trends.

Experience has shown that, given reasonably full employment and a high level of national income, domestic consumption of foodstuffs—even in the face of very high prices—is likely to run at least 15 per cent above the abnormally low levels of the late 1930's. When allowance is made for the large increase in population between 1940 and 1952, it appears that the aggregate domestic demand for foodstuffs may well run 30 per cent above the 1940 level.

In addition to the enlarged domestic demands, we have at present exceptionally large foreign requirements, the bulk of which are financed by the United States government as a part of its European relief and aid activities. (These expenditures are included in the foreign relief and rehabilitation category.) It is hoped that the foreign aid program to Europe may be reduced to negligible proportions by 1952; but given a substantial general recovery of European economic life, it is probable that there would be sizable commercial shipments of grain. Moreover, it is not improbable that conditions will necessitate food relief activities in other parts of the world. On the whole, it would appear that exports of foodstuffs in the early 1950's will be considerably higher than before the war.

Thus it seems clear that the agricultural situation will continue to be more favorable than was anticipated by most observers at the end of the war. The need for aid will accordingly be appreciably less, and there is reason to hope that the pressures for price support may be less insistent.

Federal aid to agriculture has in recent years taken two forms. The first is the support of prices under the so-called parity principle. If the foregoing view of the agricultural situation is sound, it is reasonable to expect that agricultural prices as a whole will not fall below the levels at which support is deemed indispensable (currently at 90 per cent of parity). Some commodities may, however, in a given year fall materially below parity. This may be illustrated by the

case of potatoes in 1946 and dried fruits in 1947. Variations in the supply and demand situation may of course be expected to cause marked differences among the prices of numerous farm products. Accordingly, if the price support principle should be continued, moderate expenditures might be required each year, even though the agricultural price situation as a whole is reasonably satisfactory. It should be noted here that future policy in this field has not yet been definitely settled. We shall assume, however, that a price support program will be continued. A very rough estimate of the expenditures involved in the early 1950's would be from 150 to 250 million dollars.[33]

The second type of aid is that embraced within the "soil conservation and use" program. Because of its constructive character this type of aid has gained increasing favor in agricultural circles, and it is safe to assume that it will be of central importance in the new federal agricultural program now being developed. However, if the emphasis of this program is turned further away from the objective of increasing agricultural income, the costs might be held below the level of recent years while still effectively promoting true conservation. We estimate that the level of expenditure will run somewhere between 250 and 450 millions—say 350 millions as a probable figure.

Other types of agricultural aid include grants to the states for agricultural extension services and experiment stations, expenditures under the Sugar Act of 1948, a wide variety of research activities and special services, and the overhead administration of the Department of Agriculture. Present expenditures for these purposes are running at the rate of about

[33] Policy with respect to price support is currently being debated in both congressional and agricultural circles. Though the discussions in Congress are still in the preliminary stage, it appears that the parity formula may be revised: (1) to take account of the increase in farm wage rates; and (2) to reflect the changes which have occurred in recent times in the relative position of the various agricultural products. On the whole, this would probably result in raising the parity base.

180 millions. It would seem that the expenditures in 1952 for these purposes would run around 200 million dollars.[34]

State. Activities of the states in behalf of agriculture include the agricultural extension services, experiment station work, certain activities relating to the protection and care of livestock, and the expenses of state departments or offices of agriculture. We estimate that the states will spend 125 millions for agriculture in 1952. Of this amount, 40 millions would be covered by federal grants, leaving 85 millions to be met by the states.

Local. Local governments spend small amounts for agriculture. Some payments are made for the support of county agents and extension work; these payments take the form of supplements to federal and state expenditures for the same purpose. In addition, there are a number of special districts designed to perform specific functions that benefit agriculture. Local expenditures for agriculture are estimated at 60 millions for 1952.

Other Natural Resources

Probable expenditures for the promotion and development of natural resources other than agriculture are estimated at about 1.4 billions for 1952. The minimum and maximum estimates are about 1.2 billions and 1.6 billions. Federal expenditures will account for over 90 per cent of the total.

Federal. Major federal activities in this classification include the development of atomic energy, flood control, water-power development, and reclamation and irrigation. Minor objects of expenditure include activities concerned with the nation's public lands, forest resources, and mineral resources.

Though the Atomic Energy Commission is now in its first full year of operation, available data afford a rough guide as to the probable cost in later years. Expenditures for 1948 were estimated at 444 millions in the President's budget, but

[34] We do not here include the farm tenant, production, and other loans of the Farmers' Home Administration or the loans of the Rural Electrification Administration. These transactions, especially any losses thereon, are embraced within governmental business enterprises.

the request for new funds was only 250 millions. The appropriation granted was 175 millions; in addition, contract authority of 250 millions was approved.[35] The revised budget estimate for 1948 is 476 millions; this figure includes 20 millions for expenditures by agencies other than the Atomic Energy Commission.[36] We estimate that in 1952 expenditures for atomic energy will be roughly 450 millions. The range is placed at 400 millions to 500 millions.

Flood control expenditures will doubtless also show an upward trend for some years. Mainly because of the destructive floods in the spring of 1947, an extensive supplemental program was proposed by the President in July.[37] Though the additional appropriations of 250 millions requested for 1948 were not approved, there is little doubt that expenditures in later years will be influenced by the 1947 floods. We estimate that 1952 expenditures for flood control will amount to 300 millions to 400 millions. The probable expenditure is placed at 350 millions.

Expenditures for water-power projects are estimated at 225 millions, with a range of 200 millions to 250 millions. A portion of expenditures for water-power development is closely tied in with flood control and reclamation and irrigation. For the immediate future it appears that primary emphasis will be placed on flood control. However, if the St. Lawrence Seaway project should be undertaken, expenditures for water-power development would rise sharply.

Expenditures for reclamation and irrigation are estimated at 140 millions for 1952. This is roughly 55 millions less than the estimated cost of 195 millions for the 1948 program of the Bureau of Reclamation.[38] It should be noted, however, that this program includes work on no less than 147 projects, many of which involve expenditures properly classed under flood control or water-power development. The range of

[35] Public Law 269, 80 Cong. 1 sess.

[36] *The Budget of the United States Government for the Fiscal Year Ending June 30, 1949,* p. M 39.

[37] *New York Times,* July 17, 1947, p. 13.

[38] *New York Times,* Aug. 3, 1947, sec. 1, p. 52.

expenditure for 1952 is placed at 125 millions to 160 millions.

All other federal expenditures are estimated at 100 millions. National forests and public lands account for roughly two thirds of this estimate.

State and local. The states spend moderate amounts on forest development and fish and game resources. We estimate that 65 millions will be spent by the state governments for forest and wild life activities in 1952; this excludes 6 millions of federal grants. Local governments will perhaps spend 35 millions of their own funds for comparable activities.

V. PROMOTION OF SOCIAL WELFARE

Combined expenditures of all governments for the promotion of social welfare are estimated at roughly 9.1 billions for 1952, or about 23 per cent of total cash expenditures. Of the 1952 total, the federal government would finance 1.8 billions, the states 3 billions, and local governments 4.3 billions.

Education

Public expenditures for education are estimated at 4.8 billions for 1952. Expenditures for 1940 were 2.6 billions. A distribution of the 1952 estimate by purposes, together with comparable figures for 1940, is shown in the table on page 37.

Federal. Expenditures of the federal government for education are estimated at 335 millions. Current expenditures include grants for vocational education, grants for the support of colleges of agriculture and mechanic arts, and expenses of the Library of Congress and the Office of Education, together with other minor items. In addition to these activities, our estimate assumes that—in accordance with bills now pending—grants for public school education will be approved prior to 1952 and that a moderate amount will be spent by a national science foundation.

Vocational education grants are estimated at 40 millions. This figure roughly equals the appropriations thus far made for 1948 plus the additional authorization approved in 1946.[39]

[39] 60 Stat. 775. Only a minor portion of the additional 15 millions authorized was appropriated for 1948.

During the war years expenditures were at a much higher level, as a result of special appropriations for the education and training of defense workers. The regular appropriations, however, have thus far showed little change.

FEDERAL, STATE, AND LOCAL EXPENDITURES FOR EDUCATION, ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940
(In millions of dollars)

Classification	1940	1952		
		Minimum	Maximum	Probable
Federal:				
Vocational education grants	21	30	45	40
Equalization grants		150	300	250
Other activities	'13	40	50	45
Federal total	34	220	395	335
State:				
Grants to local units	709	1,350	1,725	1,550
Operation	216	325	400	350
Capital outlays	61	100	140	125
Libraries	4	7	15	10
State total	990	1,782	2,280	2,035
Less federal grants	27	185	355	295
State total, own funds	963	1,597	1,925	1,740
Local:				
Operation, full-time day schools	1,942	3,500	3,825	3,650
Operation, summer, night, part-time schools	13	20	35	25
Capital outlays, public schools	258	350	500	450
Local colleges and universities	25	45	75	60
Libraries	48	60	80	70
Local total	2,286	3,975	4,515	4,255
Less grants	709	1,350	1,725	1,550
Local total, own funds	1,577	2,625	2,790	2,705
Total: all governments	2,574	4,442	5,110	4,780

Expenditures for miscellaneous educational activities are estimated at 45 millions. This estimate includes 20 millions for the proposed national science foundation.[40] Grants to col-

[40] H.R. 4102, 80 Cong. 1 sess., which provided for the establishment of a national science foundation, was approved by both the House and the Senate. This bill was vetoed by the President, mainly because of the nature of the administrative provisions. *New York Times*, Aug. 7, 1947, p. 1. A bill embracing the same objectives, but providing for a different administrative set-up, will probably be considered in 1948.

leges of agriculture and mechanic arts, library services, Howard University, and the Office of Education account for the bulk of the remaining 25 millions.

Federal equalization grants have not yet been approved, but the proposed program will doubtless be considered by Congress in 1948. For the purpose of our estimates, we shall assume that a bill along the lines of the one most widely discussed in 1947 will be approved. This would mean an expenditure of 250 millions for 1952.[41]

State. From the standpoint of moneys involved, grants to local units are the most important category of state educational expenditures. State grants in aid of education are definitely on the increase. From 1940 to 1945 these grants rose from 709 millions to about 830 millions; the 1946 total was over 900 millions. A further sharp upsurge will result from changes and increases approved during 1947 legislative sessions. Moreover, because of rising prices and increasing numbers of students, further substantial increases will likely be approved during sessions of 1948 through 1951. We estimate that grants to local governments will amount to 1,550 millions for 1952. This figure includes 250 millions of federal moneys, for which the states would act as transfer agent. The range is placed at 1,350 millions to 1,725 millions.

Expenditures for the operation of state educational institutions have been rising very rapidly, because of the bulge in registration resulting from the overlapping of students returning from the armed services and students just reaching college age. Even after the present abnormal period ends, the number of students will still be much higher than before the war. Larger faculties will be required and salaries will be substan-

[41] S. 472, 80 Cong. 1 sess. This bill is commonly referred to as the Taft-Thomas-Ellender bill. It was introduced by Senator Taft for himself and seven other Senators.

We do not here include any estimate for the national scholarship program for colleges and universities advocated by the President's Commission on Higher Education. This program would cost 135 millions for the first year; by 1960 the total cost would be about 1 billion dollars. *New York Times,* Dec. 22, 1947, p. 1.

tially higher. We estimate that about 350 millions will be spent for this purpose in 1952.[42]

Capital outlays for state educational institutions are estimated at 125 millions for 1952, or roughly double the 1940 total. At some institutions building programs will be under way in 1952. On the other hand, at many universities and colleges the postwar expansion of facilities will have been completed before 1952. In any event, it seems certain that for all institutions combined, construction programs will be well beyond the peak.

Local. Local expenditures for the operation of full-time day schools, including expenditures financed from federal and state grants are estimated at 3,650 millions for 1952. Expenditures for 1947 were about 3 billions, as compared with 1.9 billions for 1940.

The present upward trend in public-school costs is primarily a result of increasing compensation of teachers. In 1945, expenditures for this purpose were slightly less than 1.6 billions;[43] the comparable figure for the school year ended in 1947 was about 1,950 millions.[44] Following a comprehensive survey of recent legislation and developments, the increase for the school year 1947–48 has been estimated at 350 millions.[45] Additional but more moderate increases in teachers' compensation can be expected for the school years ending in 1949 to 1952. Further adjustments in salary schedules plus the growth factor will inevitably mean some rise. Recovery of the in-

[42] Expenditures from funds received from students attending colleges and universities under the provisions of the Servicemen's Readjustment Act are not included in our estimate of 350 millions. Since in this study such expenditures are classed under veterans' benefits, their inclusion under education would result in double counting.

[43] U. S. Office of Education, "Statistics of State School Systems, 1944–45," *Statistical Circular,* February 1947.

[44] This estimate is based on the findings of the National Education Association of the United States. The Association reports that there were 865,000 teachers for the school year 1946–47 and that the estimated average compensation was $2,250. *News Release,* April 1947.

[45] Benjamin Fine, "Teachers' Pay to Rise $400 on Average in Next Year," *New York Times,* June 28, 1947, p. 1. See also *New York Times,* Dec. 30, 1947, p. 1.

structional staff to the 1940 level before 1952 is a possibility.[46] The principal factor here is the very high birth rate of the war years.[47] We estimate that expenditures for teachers' salaries will amount to about 2.6 billions for 1951–52.

All other current costs of public day schools are estimated at 1,050 millions for 1952. The comparable total for 1945 was 871 millions, while that for 1940 was 627 millions. Included are overhead administration, textbooks and supplies, and operation and maintenance of the school plant.

Capital outlays for public schools will probably amount to something like 450 millions[48] for 1952, as compared with 258 millions for 1940. At least four factors will tend to bring outlays for school construction to a level well above prewar: (1) shifts in population during the war years, especially the sharp increase in urban population in certain areas; (2) the increase in enrollments resulting from the high birth rate of the war period; (3) the accumulated backlog in construction of the war years; and (4) the high level of costs.

Expenditures for all other local educational purposes are estimated at 155 millions. Included are the operation of summer, night, and part-time schools, operating and other costs of local colleges and universities, and city and other local libraries.

[46] In 1944–45 the instructional staff numbered 865,000, as compared with 912,000 for 1940. Recovery to the former level within the next two years is a distinct possibility, especially when one takes into account the increased enrollment in the elementary grades which is already in evidence. The extent of the increase will depend largely on whether additional teachers can be obtained.

[47] The United States Office of Education estimates that in 1947–48 first-grade enrollments will be up about 9 per cent over 1946–47. The effect of the high birth rate of the war years on enrollment will continue for many years. Since births in 1946 were at the record figure of 3,260,000, high first-grade enrollments can be expected for at least six years. *New York Times*, Aug. 3, 1947, sec. 1, p. 5.

[48] Our estimate of 450 millions a year is low, compared with certain other estimates. For example, in 1944 it was estimated that annual capital outlays of 1,347 millions would be required for the ten-year period ending in 1955 in order to remove deficiencies and meet current needs. National Education Association, "Proposals for Public Education in Postwar America," *Research Bulletin*, Vol. 22, April 1944, p. 71.

Public Health and Sanitation

Expenditures for public health and sanitation are estimated at 860 millions for 1952. The 1940 expenditure was 434 millions.

Federal. Expenditures of the federal government for all public health activities are estimated at 200 millions. The Public Health Service would account for the bulk of the total. Expenditures of this agency include a variety of services and grants under the Public Health Service Act of 1944.[49] Among other provisions, this act authorized expenditures for grants for: (1) the prevention, treatment, and control of tuberculosis; (2) the prevention, treatment, and control of venereal diseases; and (3) general public health programs, including the training of personnel for state and local health work.[50] Grants to the states for maternal and child-health services administered by the Children's Bureau are also classified under public health.

Numerous bills now pending before Congress would, if passed, materially add to federal expenditures for public health. One leading proposal would expand the activities of the Public Health Service, promote and encourage medical and dental research through grants to the states, and also through such grants provide medical care services for low-income groups. Another leading bill would establish a national health insurance system and greatly extend present public health programs. It is not unlikely that some provisions of this general type may be passed between now and 1952.

State. State activities in this classification include public health and vital statistics departments or offices, child health services, the prevention and treatment of communicable diseases (not in hospitals), food regulation and inspection, the regulation of certain professional occupations, and public health

[49] 58 Stat. 682.

[50] Another class of activity which is just beginning to be reflected in federal expenditures might be classed under public health. We refer to the grants to the states under the Hospital Survey and Construction Act of 1946; the provisions of this act are considered at p. 44.

extension services. State expenditures for public health and sanitation are estimated at 150 millions for 1952. Of this amount, about 75 millions would be financed from state funds and 75 millions from federal grants. The range of expenditure is placed at 135 millions to 165 millions.

Local. Expenditures of local governments in this classification consist mainly of city expenditures for street cleaning, garbage disposal, and other sanitary activities. Public health activities—as distinct from sanitation—account for less than one fourth of local expenditures for the combined classification. Expenditures for 1952 are estimated at 600 millions, of which perhaps 15 millions would be covered by state grants.

Recreation

Recreation is a minor function of government. Expenditures for 1952 are estimated at 320 millions, as compared with roughly 200 millions for 1940. Federal expenditures are placed at 30 millions, those of the states at 30 millions, and local expenditures at 260 millions. Park and playground facilities account for the bulk of the total.

Public Assistance

Expenditures for public assistance are estimated at 2.8 billions for 1952, or about 1.1 billions less than for 1940. The outstanding feature of public assistance payments is their change in character, as compared with prewar years. If employment conditions are generally favorable, work relief will be negligible and general relief will probably not exceed 300 millions, or something like one tenth of the aggregate requirement for public assistance. In 1940 work relief and general relief accounted for expenditures of almost 2 billions, or about one half of all public assistance. On the other hand, 1952 expenditures for categorical assistance—aids to the aged, the blind, and to dependent children—will be approximately double those for 1940. Two factors are involved here: (1) the increase in number of beneficiaries, and (2) the upward adjustment in rates because of the rise in living costs.

Federal, State, and Local Expenditures for Public Assistance, Estimates for the Fiscal Year 1952 Compared With 1940
(In millions of dollars)

Classification	1940	1952		
		Minimum	Maximum	Probable
Federal:				
Grants to states—categorical assistance [a]	271	650	800	725
Grants to states—hospitals		60	75	75
Work relief	1,466	0		
Unemployment relief	287			
National youth relief	97			
Farm and rural relief	61			
All other	320	150	250	200
Federal total	2,502	860	1,125	1,000
State:				
Categorical assistance [a]	562 [b]	1,100	1,400	1,250
General relief	335 [c]	100	150	125
Operation of hospitals	174	275	325	300
Operation of institutions for handicapped	34	50	75	60
Capital outlays	62	150	200	175
All other	28	35	45	40
State total	1,195	1,710	2,195	1,950
Less federal and local grants	300	730	905	825
State total, own funds	895	980	1,290	1,125
Local:				
Categorical and other assistance	378	600	700	650
General relief	343	160	200	180
Hospitals	204	300	350	325
Institutional and other	76	100	150	125
Local total	1,001	1,160	1,400	1,280
Less grants	422	490	635	565
Local total, own funds	579	670	765	715
Total: all governments	3,976	2,510	3,180	2,840

[a] Assistance to the aged, the blind, and to dependent children.
[b] Includes 241 millions for grants to local units.
[c] Includes 175 millions for grants to local units.

Federal. Expenditures of the federal government for public assistance are estimated at one billion dollars for 1952.[51] Of this total, 725 millions would take the form of grants to the states for assistance to the aged, the blind, and dependent

[51] This total does not include foreign relief and rehabilitation which is considered later. See p. 50.

children. The amount of these grants is increasing not only because of the factors previously mentioned, but also because a law effective October 1, 1946 increased the proportions of the benefits financed by the federal government.[52]

Grants to the states under the Hospital Survey and Construction Act of 1946[53] are estimated at 75 millions for 1952. This act authorized grants for surveys of hospital facilities and for the construction of public and other nonprofit hospitals. The authorization for surveys was 3 millions and that for construction 75 millions a year for five years. Thus far no money for construction grants has been appropriated, but an allotment of 75 millions, together with contractual obligations of not more than this amount, have been approved for the fiscal year 1948.[54]

Expenditures for all other public assistance are estimated at 200 millions. This figure includes the school lunch program and all other forms of public assistance not estimated separately. Even under the most favorable circumstances, some expenditures for miscellaneous relief purposes such as drought relief and disaster relief can be expected.

State. Expenditures of the states for public assistance include payments to the aged and other special groups, and the operation and maintenance of hospitals[55] and institutions for the handicapped.[56] State expenditures in this classification are estimated at about 2 billions, including 825 millions covered by grants.

Categorical assistance payments are estimated at 1,250 millions, of which 725 millions would be covered from federal funds. In turn, something like 450 millions of state expendi-

[52] 60 Stat. 991. These provisions were extended to June 30, 1950 by Public Law 379, 80 Cong. 1 sess.

[53] 60 Stat. 1040.

[54] Public Law 165, 80 Cong. 1 sess., p. 9.

[55] In this study state and local hospitals are classed under public assistance rather than public health. By far the largest portion of state expenditures for hospitals are for special hospitals, especially for the insane and the tubercular. On the other hand, most local expenditures are for general hospitals.

[56] Including the blind, the deaf and mute, and the feeble-minded.

tures may take the form of grants to local governments.[57] General relief payments by the states are estimated at 125 millions, of which perhaps 75 millions would take the form of grants.

Operating costs of state hospitals are estimated at 300 millions for 1952. The comparable figure for institutions for the handicapped is 60 millions. Expenditures for these purposes will be strongly influenced by the number of patients and personnel requirements.

Outlays for the construction of hospitals and eleemosynary institutions of all kinds are estimated at 175 millions. This figure embraces the entire 75 millions of federal grants for hospitals referred to above. Since some of these funds will probably take the form of grants to local units, we shall here assume that 40 millions will fall in this category. In the absence of any clear indication, it is assumed that the remainder will take the form of direct state expenditures.[58]

Local. Expenditures of local governments for public assistance are estimated at about 1.3 billions for 1952; of this amount, 565 millions would be covered from grants. Categorical assistance and operation, maintenance, and construction of hospitals are the most important objects of expenditure.

Social Security Administration

Expenditures for social security administration are estimated at 80 millions for 1952. Federal grants to the states and the District of Columbia for the administration of unemployment compensation are the largest item. These grants are estimated at 65 millions for 1952. Despite the views of some state officials that more liberal federal appropriations should be made for administering unemployment compensation, the appropriation for 1948 was held to roughly 58 millions. The current level of appropriations, it is said, represents only a

[57] This estimate is based on data for 1945; in that year more than 36 per cent of state payments for categorical assistance consisted of grants.

[58] Though the situation is not clear, some of the moneys involved will probably be spent on state hospitals, and a portion will also be allocated to nonprofit hospitals.

fraction of federal collections from the unemployment compensation tax,[59] which is often regarded as the source of funds for the grants. Other federal expenditures for social security administration are estimated at 15 millions. This figure includes overhead administration of the Social Security Board and salaries of the Bureaus of Public Assistance and Employment Security, together with miscellaneous expenses.

The estimate of 80 millions does not include expenditures for the administration of the old-age and survivors insurance system payable through the old-age and survivors insurance trust fund. Nor does it include the administrative expenses of the Railroad Retirement Board, which we regard as chargeable against revenues from the railroad retirement taxes. These administrative expenses are considered in Chapter VII.

Housing

Expenditures for housing are estimated at 240 millions. Of this amount, 140 millions would be spent by the federal government. The latter estimate assumes that a bill roughly comparable to the Taft-Ellender-Wagner bill[60] will be approved within the next few years. Direct housing aids would perhaps account for over 100 millions of the federal estimate; the bill just referred to would provide direct aids of 105 millions. In our summary tables we have assumed that the entire 140 millions would be spent directly; that is, no part would take the form of grants to state and local governments. Since the nature of the financial provisions of any federal housing act that might be approved are uncertain, this assumption is perhaps somewhat arbitrary.

State housing aids are estimated at 50 millions and local aids at 50 millions. Both figures, which are very rough estimates, are for costs that would be reflected in state and local budgets for 1952.

[59] Collections for the year ended June 30, 1947 were 186 millions. For further discussion, see p. 79.

[60] S. 866, 80 Cong. 1 sess.

VI. INTEREST ON PUBLIC DEBT

Cash interest payments are estimated at roughly 5.3 billions for 1952, or almost 13 per cent of combined expenditures for all functions. The comparable figures for 1940 were 1.5 billions and 8.6 per cent.[61] Federal cash interest for 1952 is estimated at 4.7 billions and combined state and local interest at 575 millions.

Federal. Interest payments on the federal debt may be influenced either by a change in the average rate of interest or by a change in the amount of debt. With respect to the former, it would seem that the trend would be moderately upward, assuming the continuance of a high level of business activity and a growing demand for loanable funds. There has already been a slight upward trend, in line with the general firming of interest rates. Moreover, the average cost to the federal government is affected by changes in the distribution of the debt. In the past few years the proportion of the total represented by short-term obligations has decreased appreciably. In our view a rise of something like two tenths of 1 per cent is not unlikely. Applied to the total debt on which interest is paid in cash, this would involve an increase of something like 400 million dollars a year.

To estimate the probable magnitude of the public debt as of 1952 would require a thorough appraisal of fiscal policies in relation to the level of national income during the intervening years. This is not the place to make such an appraisal. All that one can do here is to indicate how much the interest cost would be changed by possible fluctuations—up or down—in the total debt. If national income is maintained throughout the intervening years at or above present levels, and if taxes are not greatly reduced, one could hope for a substantial reduction in the outstanding debt in the next five years. On the other hand, if we should run into a considerable recession in

[61] In addition to the amounts mentioned, substantial sums for noncash interest are commonly included in governmental expenditures. For 1952 the interest credited to social security and other trust and investment funds, plus the excess of interest accruals on savings bonds over interest included in retirements, will probably amount to well over one billion dollars.

business activity, or if taxes were substantially curtailed, we could easily have a return of deficits of substantial proportions.[62] In the face of the foreign aid program and the insistent demands for tax relief, it would not be safe to assume that a substantial reduction in debt is certain to occur.

The estimates which we here use are based upon the following assumptions with respect to the reported interest-bearing debt: (1) a continuance of the debt at the present level of about 255 billions; (2) an average annual decrease over the next five years of about 3 billions, bringing the total down to 240 billions; and (3) a net increase in the debt in the five-year period of 10 billion dollars. On this basis, the debt on which interest would be paid in cash would probably fall between 200 billions and 230 billions. We shall here use the intermediate figure of 215 billions as the probable.[63] At 2.2 per cent the total for cash interest payments thus becomes roughly 4.7 billions.[64]

State. The estimate of 145 millions for state interest payments represents a substantial rise over recent figures. A sharp reversal in the recent trend in state debt is now occurring. We estimate that the combined debts of the state governments exclusive of debts of public-service enterprises serviced from their earnings, will increase from 2,150 millions for 1946 to 5,750 millions for 1952. This enormous increase will result mainly from the issuance of soldiers' bonus bonds, which are conservatively estimated at 3 billions. However, since some of these bonds will probably have been retired by 1952, the

[62] It should not be forgotten in this connection that our tax system is so geared that the yield fluctuates widely with changes in the total national income.

[63] A large portion of the reported interest-bearing debt consists of special and other issues held by federal trust and investment funds on which interest is not paid in cash. On June 30, 1947 the total was 32.8 billions.

[64] In arriving at this estimate, no correction has been made for interest accruals on savings bonds in excess of interest included in retirement of such bonds. Retirements of maturing savings bonds will be substantial in 1952, and the cashing of unmatured obligations will help swell the total. Though the possibility of excess accruals in 1951–52 is recognized, we believe the procedure here adopted gives the best picture for a year in the first half of the decade of the 1950's. Because of the enormous maturities in 1953–55, current accruals in these years are certain to fall far short of the deferred interest included in retirements.

net increase on account of this debt may be somewhat smaller. The remaining increase of upwards of 600 millions embraces state issues for all other purposes except public-service enterprises. The average interest rate on the increment in debt is placed at 2 per cent.

Local. The estimate of 430 millions for local interest payments assumes a moderate increase of 1.5 billions to 2 billions in outstanding debt. The average interest rate on new borrowings is placed at 2.4 per cent. As in the case of the states, only minor changes from the rates on recent borrowings are assumed. The estimate for local interest does not include that payable from the earnings of public-service enterprises.

VII. GENERAL GOVERNMENT

Expenditures for general government are estimated at 1.9 billions for 1952, or almost 5 per cent of cash expenditures. Comparable figures for 1940 were 1.1 billions and 6.3 per cent.

Federal. Legislative, judicial, and executive activities classed under general government will account for federal expenditures of 490 millions in 1952, according to our estimates.[65] Financial administration is the most important component. The federal government will spend something like 325 millions for this purpose in 1952. Of this amount, 225 millions or slightly more will be spent for collecting the revenue.[66] Public supply, personnel, and property will account for federal expenditures of perhaps 150 millions to 175 millions. Acquisition of public buildings and sites is by far the largest item, accounting for one half or more of the latter estimate.

Federal expenditures for foreign relations are estimated at 175 millions for 1952, or somewhat less than the indicated level of expenditures for 1948. Our estimate assumes that expenditures for the information and cultural program will be roughly the same as at present.

[65] The general government classification here used differs appreciably from that used in preparing the President's budgets for 1948 and 1949. A number of items there classed under general government we have included under other functions.

[66] Appropriations for collecting the revenue amount to 221 millions for 1948; this figure includes both internal revenue and customs.

State. General government expenditures of the states are estimated at 305 millions for 1952. Of this amount, perhaps 150 millions to 175 millions will be spent for financial administration. Outlays for general government buildings will no doubt amount to something like 40 millions to 50 millions. Salary adjustments will also be an important factor making for increased expenditure.

Local. Local expenditures for general government are estimated at 960 millions, an increase of roughly one half over 1940. Many urban governments will doubtless show a much larger relative increase. On the other hand, expenditures of numerous county and other local governments may rise by less than one half.

VIII. FOREIGN LOANS AND RELIEF

Until recently it was hoped that the foreign loan and relief activities of the United States government would largely disappear within two to three years after the end of the war. However, as a result of continued economic disorganization in other parts of the world, it now appears that the United States will continue for at least several years to grant large funds for foreign relief. Under the European aid program, the estimated amounts for the next four years range from 12 billions to 17 billions, with the annual amounts gradually declining. Though it is hoped that by 1952 further European aid from the federal government will not be required and that such foreign assistance as may be required thereafter may be obtained exclusively through private financial channels, one cannot be certain that the European situation will be sufficiently stabilized at that time to eliminate all necessity for further aid. Political as well as purely economic considerations are involved. In any case, it appears highly probable that the United States will continue to assume substantial costs in the control and rehabilitation of Germany. Close students of this problem do not anticipate that we can get out from under the German obligation as early as 1952.

It also appears probable that substantial aid will be fur-

nished to other parts of the world. The present program already includes a fairly large amount of aid for China. Whether something will in time be included for other Asiatic countries remains to be seen. With respect to South America, consideration of an aid program has been deferred but not eliminated as a possibility.

In the light of the foregoing, we would conclude that the range of expenditures for foreign aid in 1952 might fall between 500 millions and 3 billions, with perhaps 1 billion dollars the probable figure.

IX. MISCELLANEOUS EXPENDITURES

Expenditures of all governments classed as miscellaneous are estimated at 920 millions for 1952. The federal figure of 350 millions covers Indian affairs, net payments[67] on account of government life insurance, net cash payments for employees' retirement, the federal grant to the District of Columbia, other minor items, and an allowance for contingencies. State expenditures, which are estimated at 160 millions, include payments to retired employees and certain undistributed grants—among other items. The local estimate of 410 millions is relatively much larger than the federal and state estimates. The size of this item is to some extent a result of imperfections in local data used as a basis for our estimates.

X. GOVERNMENTAL BUSINESS ENTERPRISES

Activities of government that are in the nature of business enterprises will require 300 millions of funds from general sources in 1952, according to our estimates. Federal expenditures are estimated at 300 millions and those of local governments at 60 millions. The negative estimate of 60 millions for the states represents mainly the net contribution of liquor monopolies to general revenues.[68] The estimates for each of the three levels of government are on a net basis.

[67] That is, cash payments in excess of premiums and other cash receipts.

[68] The estimate of 60 millions is much lower than the annual contributions in 1946 and preceding fiscal years. Because of the sharp decline in consumption in 1947, there is reason to believe that the state liquor monopolies will be much less profitable than during the war period.

The federal estimate assumes that postal operations will either be self-sustaining or will result in no more than a very small deficit. Another assumption is that the 16 state liquor monopolies will continue to be profitable and that substantial profits from their operations will become available for general state purposes. On the other hand, the need for large general revenues to cover operating deficits of certain municipal enterprises—especially the New York City transportation system—will doubtless continue.[69]

The most striking conclusion suggested by this chapter is that roughly one half of estimated public expenditures for 1952 will be either an outgrowth of past wars or will be incurred for the purpose of ensuring the defense of the nation. Expenditures arising from past wars include veterans' benefits, all but a small part of federal interest payments, and foreign aid and relief, together with minor items. In 1940 roughly one seventh of total public expenditures were attributable to national defense and past wars.

The bulk of the remaining expenditures will be incurred for the welfare, developmental, and protective (other than military) activities of government. Our estimates indicate that these three classifications combined will account for over 40 per cent of total expenditures for 1952, as compared with almost 70 per cent for 1940. The marked decline in the relative importance of these broad classes of expenditure is mainly a result of two factors: (1) the sharp increase in defense costs and other expenditures related to wars; and (2) the abnormally high level of public assistance expenditures in 1940.

[69] The estimates in this chapter have not included any allowance for debt retirement. It would of course be wholly illogical to include debt retirements in a study of expenditures by functions. Such a procedure would clearly involve double counting over a period of years. For example, if funds were borrowed in 1940 and spent for national defense and the loan is repaid in 1952, it is obvious that the amount involved should be counted only as a national defense expenditure in 1940.

CHAPTER III

THE REVENUE PROBLEM

The foregoing analysis of the influences affecting governmental expenditures has indicated that by 1952 the total for federal, state, and local governments combined is likely to be roughly 40 billion dollars. Of this amount, approximately 26 billions would be financed by the federal government and 14 billions by state and local governments. Since this projected total is some 6 to 8 billions less than estimated expenditures for the present fiscal year, the outlook on the surface may appear reassuring. Inasmuch as total revenues are currently running substantially above expenditures, need there be any concern about the situation as projected for 1952?

Before answering this question, one must consider two factors in the situation which may profoundly alter the picture. The first relates to the fact that we are now in the midst of an intense boom, resulting in a national income higher than can safely be counted on as an average over a period of years. The second is the widespread conviction that taxes must be sharply reduced. In the present chapter we shall attempt to indicate the possible impact of these factors upon revenues.

I. CHANGES IN NATIONAL INCOME AND TAX REVENUES

Attention is first directed to the effects of even moderate changes in production and employment on the volume of national income. A reduction of only 10 per cent in production and employment would involve—at present levels of activity and current prices—a reduction in national income of close to 20 billion dollars. A reduction of 20 per cent would affect national income more than proportionately, because of the greater ramifications throughout the economy; the over-all reduction in national income might well run as high as 50 to 60 billions. A 20 per cent decrease in the level of production and employment would represent a depression of only minor

proportions. It would, for example, be of lesser magnitude than the recession that was predicted for 1947 by many forecasters. Though it is hoped that a much higher degree of business stability may be achieved in the future than has been the case in the past, there can be no certainty that we shall not again experience a major depression.

One may conveniently gauge the relation of national income to tax revenues by asking: How would governmental revenues in the current fiscal year have been affected if national income had been 10 or 20 per cent below the level that has thus far prevailed? The all-important fact is that we have a high-geared tax system, and in consequence revenues are more than proportionately affected by a given decrease—or increase—in national income. Though it is impossible to present precise estimates, a 10 per cent reduction in national income would probably mean a 12 to 14 per cent decline in revenues, or 7 to 8 billion dollars; and a 20 per cent decline in national income would perhaps involve something like a 30 per cent drop in revenues, or 16 to 18 billion dollars. With only a 10 per cent slump in national income, the present estimated federal surplus would have been replaced by a deficit, or at best a precarious balance. With a 20 per cent lower national income, we would have a federal deficit in excess of 10 billion dollars.

If one is to be realistic about the fiscal situation, it must be conceded that the extraordinary level of business activity existing in 1947, with employment at virtually wartime levels, cannot be counted on permanently. Even a comparatively modest depression would change the fiscal picture from good to bad with startling suddenness.

In the revenue estimates presented in the following chapters, we shall use a national income of 175 billions as a base. This figure is only about 12 per cent below the present level. Even allowing for the growth factor, this is a high figure for a representative or average year.

THE DEMAND FOR TAX REDUCTION

In the first two years following the war, taxes have not been reduced appreciably.[1] To meet the financial exigencies of this difficult period, the American people have been asked to continue their support of government on virtually a wartime basis. During recent months, however, demands for substantial tax reduction have become increasingly insistent. These demands, as we shall see, come from all groups in the body politic.

In our projection of probable expenditures, account was taken of the demands of the people for governmental services. Now we must take account of public attitudes with respect to taxes. There is an apparent conflict between the demand for public services and the desire for tax reduction.

The demand for tax reduction is based upon a variety of considerations. First, there is the view that the American people cannot reasonably be expected to bear permanently a burden of taxes comparable to that existing in time of war. This consideration implies the necessity of a reduction of federal taxes all along the line. A second argument is that a reduction of taxes is essential to the maintenance and improvement of the consuming power of the masses of the people. A third general consideration is that high taxes impede investment, especially in risky undertakings. In order to appreciate the magnitude of a potential tax reduction program, it is necessary to indicate various specific proposals that are now under discussion.

1. *A sharp reduction in taxes on low incomes.* The proposal commanding the widest popular support is that taxes on low incomes should be sharply reduced or eliminated. Because of the marked rise in the cost of living, many people doubt there is any justification for taxing those in the lowest net income brackets. In numerous instances taxes have been paid at the expense of savings or have involved drawing on prior savings. Though the immediate goal is to increase disposable

[1] The only important exception is the federal excess profits tax, which was repealed as of January 1, 1946. The decline in federal tax revenues, which resulted mainly from repeal of the excess profits tax, was offset in part by the upward trend in state and local tax revenues.

income of those with small incomes, underlying this proposal is the belief that tax reduction is essential in order that consumption and living standards may be maintained. Closely related is the view that a rising level of consumption is essential to the continuance of high-level employment.

Tax relief for those with small incomes might take one of three forms: (1) an elimination of income taxes for persons with low taxable net incomes; (2) an increase in personal exemptions; or (3) a deduction from the amount of tax, as computed at prevailing rates. Under the first approach, canceling of income taxes of all persons with taxable net incomes of not over \$1,000 might possibly be justified. If this step should be taken, a federal tax loss of at least 2.4 billion dollars would be involved.[2]

Under the second approach, personal exemptions might be increased from the present figure of \$500 to \$600 or \$700. An increase from \$500 to \$600 would mean combined exemptions of \$1,200 for a married couple and \$2,400 for a married couple and two dependent children. A uniform exemption of \$600 applicable to all taxpayers regardless of income would mean a revenue loss of over 1.6 billion dollars. The larger figure of \$700 would involve a loss of over 3 billion dollars.[3]

Under the third approach, a stated or determinable amount might be deducted by the taxpayer from the computed tax. Thus, the recent proposal of the President would provide for a cost-of-living adjustment of \$40 for each taxpayer plus a like amount for each dependent. The revenue loss is estimated at 3.2 billions.[4]

[2] The estimates for revenue losses in this chapter are based on a national income including corporate profits taxes of 175 billion dollars. The corresponding figure for income payments would be roughly 165 billions. At the present level of national income, the revenue losses would of course be larger.

[3] These estimates are comparable to those presented in *Individual Income Tax Reduction,* Hearings Before the Senate Committee on Finance, 80 Cong. 1 sess., p. 30.

[4] *New York Times,* Jan. 8, 1948, p. 4. A bill embracing this proposal was introduced in the House of Representatives on January 14 by Representative Dingell. *New York Times,* Jan. 15, 1948, p. 1.

The cost of living, or consumption, argument obviously also applies in varying degrees to all whose taxable incomes are below, say, \$4,000. A very sharp cut for the first bracket of \$2,000, say from 19 per cent to 6 per cent, would involve a revenue loss of about 4.7 billions; for a reduction to 10 per cent the loss would be about 3.3 billions.[5] For the next bracket —\$2,000 to \$4,000—a sharp reduction from the present 20.9 per cent to 10 per cent would involve a loss of over 700 millions, while a cut to 14 per cent would mean a loss of about 450 millions. Smoothing the rate schedule for the next bracket —\$4,000 to \$6,000—might involve a further loss of 250 to 300 millions. At the lower rates these reductions would aggregate roughly 5.7 billions, and at the higher rates 4 billions.

2. *A substantial cut in middle-bracket rates.* The argument for tax reductions for those with incomes of from, say, \$6,000 to \$25,000 relates more largely to the impairment of savings than to the reduction of consumption. Those who press the claim of the middle brackets for tax reduction contend that present taxation unduly restricts the flow of investment funds into additions to plant and equipment. Tax reductions in these brackets are particularly important from the point of view of the supply of equity or risk capital.[6] It is believed that the supply of investment money, especially for undertakings involving substantial risk, may prove inadequate during the next few years.

At present the rates for the middle brackets range from 28.5 per cent on the increment between \$6,000 and \$8,000 to slightly over 56 per cent on the increment between \$22,000 and \$25,000. If these rates were reduced to 16 per cent and 34 per cent, with appropriate gradations for the brackets be-

[5] These estimates assume that all taxable income in the first \$2,000 bracket remaining after freeing those with taxable incomes of \$1,000 or less would be taxed at the rates mentioned. If the taxes of those with taxable net income of \$1,000 or less should be canceled, a notch provision applicable to taxable net incomes just above \$1,000 would be necessary. The notch provision would mean a substantial increase in the revenue loss.

[6] The bulk of the savings of those in the lower brackets becomes available for investment only in seasoned securities, particularly bonds.

tween those mentioned, a revenue loss of well over 1 billion dollars would be involved.

Reductions in middle-bracket rates as sharp as those mentioned would obviously call for substantial cuts in the brackets ranging from $25,000 to $50,000. Rate gradations ranging from 36 per cent for the $26,000–$32,000 bracket to 42 per cent for the $44,000–$50,000 bracket would involve a further loss of roughly 450 millions.[7]

3. *A top effective rate of 50 per cent.* At present the top bracket rate is 86.45 per cent, though the over-all effective rate can in no case exceed 85.5 per cent of net income. The arguments against rates which absorb the bulk of large incomes are two-fold in character. The first is that the small portion of income remaining after taxes tends to destroy incentives and does effectively destroy the possibility of accumulating a substantial fortune. The second is that the great reduction of savings margins in the higher income levels serves to dry up sources of funds formerly available for investment and for the support of educational and philanthropic institutions. Under present conditions, many wealthy individuals are drawing upon principal.

At present, the average effective rate on taxable net income reaches 50 per cent at a little less than $48,000. Adoption of a maximum effective rate of 50 per cent would involve a revenue loss of approximately 750 million dollars.

Under an alternative plan, the top bracket rate might be limited to 50 per cent, with a somewhat lower average effective rate. This proposal is based on the thought that it is the *top* bracket rate rather than the average rate which directly affects incentives. On the basis of the present rate schedule, the revenue loss under this plan would be slightly over 1 billion dollars.[8]

[7] Including taxable income between $25,000 and $26,000, this estimate would probably be in excess of 475 millions.

[8] Of the two estimates, only the first—750 millions—can be added to the previous estimates in order to get the approximate combined revenue loss. The element of overlapping is in this case very slight; this follows from the fact that the average effective rate of 50 per cent is reached at just under

4. *Equity and the community property principle.* Certain western and southwestern states have long had what is known as the community property system. Underlying this system is "the concept of the marital relationship—the doctrine that since both spouses contribute to the economic gains which accrue to the couple after marriage, they have equal rights to them."[9] As a result, married taxpayers in these states having taxable incomes in excess of $2,000 pay lower taxes than those with the same incomes in other states. This problem was not regarded as of major importance as long as tax rates were moderate and only eight or nine states had the community property system. Since 1940, however, the system has been extended to Pennsylvania,[10] Michigan, Nebraska, and Oregon, and other states are giving the matter serious consideration.

A tax structure that will yield equitable results, regardless of state provisions governing the allocation of income to a spouse, has come to be regarded as a prime necessity. The method most widely suggested would involve a division of income between married taxpayers in all states. The Treasury has estimated that if such a splitting of income were made optional in all states, there would be a revenue loss of about 750 million dollars.[11]

5. *Reduction of corporate income tax rates.* Prior to the war the rate for the corporate income tax was 19 per cent, but credits for dividends and special rates for small incomes brought the average effective rate to a somewhat lower figure. During the war the basic rate was raised to 40 per cent, with

---

$48,000, while our previous estimate took into account net income up to $50,000. Because of considerable overlapping, the larger estimate of over one billion should not be added to that for the estimated loss resulting from a reduction in rates on incomes in the range of $25,000 to $50,000.

[9] U. S. Treasury Department, *The Tax Treatment of Family Income* (mimeo.), June 1947, p. 1. There is considerable variation in detail among the systems in use in the several states.

[10] The Pennsylvania law was declared unconstitutional by the Supreme Court of that state on Nov. 26, 1947.

[11] The exact figure is 743.5 millions. U. S. Treasury Department, *The Tax Treatment of Family Income,* p. v. The Treasury's estimate assumes income payments of 166 billions.

somewhat lower rates for small incomes. The basic rate has since been reduced to 38 per cent.

Demands for a reduction in corporate income tax rates are based principally on the belief that the corporate income remaining after taxes will be insufficient to cover minimum dividend requirements and provide for expansion. This problem is not acute so long as peak volume production exists; it might become serious with any considerable decline in the rate of business activity. It is emphasized in this connection that the "break-even point" in corporate operations is now very much higher than it was before the great advance in wage rates and raw material costs occurred.

A reduction in the basic rate to the prewar level, with corresponding reductions for small incomes, would involve a revenue loss of something like 4 billion dollars. This figure is based on an effective tax base of 20 billions before federal income tax—a figure well below the present exceptionally high level.

A related proposal is that taxpayers should be permitted greater discretion with respect to depreciation allowances. This argument is based upon the fact that replacement costs have risen sharply. Since such a change would presumably be at the expense of a reduction in corporate tax rates of several percentage points, the loss of revenue need not be figured separately.

6. *Lower taxes on consumption.* The major reason advanced in favor of a marked reduction in or the elimination of federal taxes on consumption is that such taxes fall most heavily on persons with low incomes. The items taxed include —in addition to furs, jewelry, and other luxuries—automobiles, trucks, automobile accessories, gasoline, refrigerators, radios, transportation, communications, and liquors and tobacco. For revenue reasons most of those favoring repeal of federal excises would agree to continue the taxes on liquors and tobacco, and perhaps gasoline. If all other federal excises were discontinued, the revenue loss would be approximately 3 billion dollars.

Those favoring minimum reliance on consumption taxes by the federal government regard state and local excises as equally undesirable. In particular, general or retail sales taxes are regarded with disfavor and their repeal is strongly urged. If all state and local sales taxes other than those on liquor and tobacco and gasoline were repealed, the revenue loss would run from 1 to 1.5 billion dollars.

If all the tax reduction proposals discussed above were adopted, the loss of revenue—with allowance for overlapping—would be somewhere between 16 and 20 billion dollars. Of this total, roughly 15 to 18 billions would be federal revenues. It should be emphasized that these estimates are based on a national income of 175 billions. Since at this level of income the federal budget would be approximately in balance at present tax rates, it follows that any such series of tax reductions as the above would, if adopted, leave us with an enormous deficit.

In the light of this analysis of the two major factors affecting government revenues, the outlook for fiscal stability over the next five years is in reality far from reassuring. On the one hand, extensive reductions in taxes could result in a large deficit even with national income continuing at a high level. On the other hand, a moderate reduction in national income, with tax rates remaining at present levels, would produce a substantial deficit. Moreover, if national income should decline sharply, demands for tax reduction would become the more insistent. At the same time, certain types of expenditure would expand rapidly.

Since the government is committed to the principle of maintaining fiscal stability, the alternatives before the American people are as follows: (1) to forego a substantial portion of the tax reductions desired; or (2) to restrict the level of public expenditures. The necessity of choosing between these alternatives could be escaped only in the event that a solution is found to the problem of business fluctuations and if we should continue to have a rapidly rising national income.

If expenditures should remain at as high a level as the trends discussed in preceding chapters indicate, what general level of taxes would be necessary to make ends meet? In the next three chapters we shall endeavor to show what would be involved in a tax system to meet such a level of expenditures.

CHAPTER IV

FEDERAL TAXES AND OTHER REVENUES

In this chapter we shall indicate the kind of a federal tax system that would be necessary in the years ahead if federal expenditures are at the 26 billion dollar level indicated in Chapter II. How might the projected requirements be apportioned among the several sources of federal revenue? What tax rates would be necessary to yield the amount of revenues required to maintain a balanced budget?

Several assumptions underlying this analysis should be made clear at the outset. First, it is assumed that no new federal taxes of major revenue importance will be adopted. Second, it is assumed that such rate adjustments as may be feasible by reason of reduced expenditures over the next five years will be restricted mainly to income taxes. Third, the tax figures for 1952 are based on an assumed national income of 175 billions before deduction of corporate income taxes. As indicated in the preceding chapter, this is a high figure for a representative or average year.

The revenue pattern at which we arrive for the year 1952 is shown in the table on page 64. For purposes of comparison, data are also presented for the years 1940 and 1946. It should be kept in mind that the revenue figures in this study are presented on a cash basis.

I. INCOME TAXES

Under the revenue program indicated on p. 64, the federal government would rely on income taxes for something like 17.4 billions[1] for the fiscal year 1952. Income taxes would represent about two thirds of all federal revenues other than pay-roll taxes credited or transferred to trust funds. The total of 17.4 billions is over eight times income tax collections for the fiscal year 1940, the last prewar year not affected by

[1] This figure is net after refunds. Throughout this study tax refunds are treated as deductions from revenues rather than as expenditures.

the impending war. Income tax collections for 1940 were 2.1 billions, or roughly 40 per cent of federal revenues.

Since the distribution of aggregate federal income taxes between the individual and corporate taxes for a year four or five years hence is surrounded with considerable uncertainty, two different approaches will be considered. Under the first approach, it will be assumed that the present form of income-tax structure will be retained, and that a high-rate corporate

FEDERAL TAXES AND OTHER REVENUES, ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940 AND 1946
(In millions of dollars)

Source	1940	1946	1952
Internal revenue taxes:			
Corporate income tax[a]	1,139	12,553	5,000
Individual income tax[a]	982	18,704	12,400
Estate and gift taxes	360	677	975
Liquor taxes	624	2,526	2,000
Tobacco taxes	608	1,166	1,400
Manufacturers' excises	447	923	1,650
Retailers' excises		492	300
Stamp taxes	39	88	85
Miscellaneous taxes	157	1,490	850
Unemployment tax[b]	106	179	190
Capital stock tax[c]	133	352	
Total internal revenue taxes	4,595	39,150	24,850
Less refunds[d]	—74	—3,104	
Less adjustment[e]	—14	+280	
Net total internal revenue taxes	4,507	36,326	24,850
Customs less refunds	332	426	550
Total taxes	4,839	36,752	25,400
Miscellaneous receipts	322	3,256[f]	640
Total taxes and miscellaneous receipts	5,161	40,008	26,040

[a] The distribution between corporate and individual income taxes for 1952 is that under the first approach. See p. 65. The amount shown for the corporate income tax for 1940 includes 18.5 millions from the declared-value excess profits tax; the figure for 1946 includes 7.9 billions of excess profits taxes.

[b] Includes only the federally collected portion of the tax for unemployment compensation purposes imposed on employers of eight or more persons.

[c] This tax was repealed with respect to years ending after June 30, 1945.

[d] Refunds are not available by classes of taxes.

[e] Data for internal revenue collections by classes are available only on the reports of collections basis. This adjustment is necessary to bring the total into conformity with that in the U. S. Treasury Department, *Combined Statement of Receipts, Expenditures and Balances of the United States* (1940) and (1946).

[f] Partly estimated.

income tax will continue to be imposed. Under the second approach, a sharply different income tax structure is envisaged, with the corporate income tax relegated to a relatively minor position.[2]

First Approach

Our estimates under the first approach are 5 billions for the corporate income tax and 12.4 billions for the personal income tax.

Corporate income tax. The figure of 5 billions is based on corporate profits of 20 billions and an average effective rate of 25 per cent. The estimate of 20 billions we shall regard as the actual base for the federal tax.[3] That is, this total is assumed to be net of those state income taxes which are deductible for federal tax purposes, but it includes the portion of intercorporate dividends not offset by the 85 per cent credit.

The total of 5 billions assumes a reduction of about 11 percentage points in present rates for the corporate income tax. That is to say, the basic rate which is now 38 per cent[4] would be reduced to 27 per cent. The comparable average effective rate on all taxable corporate income would be about 25 per cent, as compared with roughly 36 per cent at present.[5] The difference between the basic rate and the average effective rate is accounted for in part by the preferential rates for incomes of $50,000 or less to which we next refer. The additional 2

[2] With perhaps only a single important exception, treatises on postwar tax policy have concluded that the corporate income tax should be de-emphasized or discontinued. The exception here referred to is The Twin Cities Research Bureau, *Postwar Taxes* (1944), pp. 12 ff.

[3] Before selecting 20 billions for corporate profits before federal income taxes, profits and related data for the past decade were carefully examined. This figure is below the level of 1942–45, when heavy excess profits taxes were imposed. It is also lower than profits for 1946. With the national income at 175 billions, profits after federal income taxes would represent only a slightly larger proportion of national income than in 1940.

[4] The normal rate is 24 per cent and the surtax is 14 per cent.

[5] In an analysis made by the Treasury Department in 1945, the indicated difference between the basic rate and the average effective rate was roughly 2 percentage points. See *Revenue Act of 1945*, Hearings before the Senate Committee on Finance, 79 Cong. 1 sess., p. 46. The difference here referred to will of course be influenced by whether or not the additional rate of 2 percentage points for consolidated returns is continued.

percentage points for incomes reported on consolidated returns is of course an offsetting factor.

Rates for corporations with incomes of $50,000 or less would be reduced by perhaps 8 to 10 percentage points. Present rates are 21 per cent on the first $5,000, 23 per cent on the next $15,000, 25 per cent on the next $5,000, and 53 per cent on the next $25,000. The latter is a "notch" rate. It results in an increasing average effective rate on total incomes in the range of $25,000 to $50,000; for example, the average effective rate on a net income of $49,900 is 37.97 per cent.[6]

Personal or individual income tax. The total of 12.4 billions for individual income taxes seems enormous, when compared with prewar figures. It is over 12 times individual income tax collections in 1940 and more than two and a half times as large as all federal taxes for that year. If income payments should amount to 165 billions,[7] federal personal income taxes would represent roughly 7.5 per cent of the combined money incomes of the people.

It does not follow, of course, that the average rate on taxable income would be as low as 7.5 per cent. Considered together, personal exemptions, incomes not returned because they are below the exemption levels, deductions on taxable returns, exempt income, and unreported income result in an enormous difference between income payments and taxable income. For example, the ratio of taxable income to income payments was 32 per cent for 1942. Income payments for

[6] The present notch bracket of $25,000 is inordinately large and the notch rate is extremely high. The marginal rate on income between $25,000 and $50,000 is 53 per cent. This results from the substantial spread between 23 per cent, the average rate on an income of $25,000, and the basic rate of 38 per cent.

[7] In the present study we use the concepts income payments and national income employed by the Department of Commerce prior to July 1947. Our reasons for not using the new concept of personal income are: (1) various references are made to Treasury estimates based on income payments; (2) monthly data which permit the derivation of figures for completed fiscal years and portions of a year are available only for income payments; and (3) the concept of income payments is more generally understood. The differences between "income payments" and "personal income" are fully set forth in U. S. Department of Commerce, *National Income: Supplement to Survey of Current Business*, July 1947.

that year were 117.3 billions,[8] and taxable income was only about 37.5 billions.[9]

In recent years the ratio of taxable income to income payments has increased. Investigations by the Treasury Department indicate that with income payments at 166 billions, taxable income of 69 billions or about 41.5 per cent of income payments can be expected under the present tax law.[10] Since the comparable proportion for 1942 was 32 per cent, the relative increase is roughly one third. The sharp rise in income payments is the major reason for this increase. Given a fairly low level of exemptions, a relatively large portion of any increase in income payments will be reflected in taxable income. Reductions in exemptions also contributed to the rise in the ratio.

The ratio of taxable income to income payments for the early 1950's will be strongly influenced by the level of national income and personal exemptions. In our approximations, it will be assumed that income payments will be 165 billions and that exemptions will remain at present figures. On this basis, a ratio of taxable income to income payments of 42.5 per cent would seem to be a reasonable expectation.[11] This would mean

[8] U. S. Department of Commerce, *Survey of Current Business,* February 1946, p. 8.

[9] U. S. Treasury Department, *Statistics of Income 1942,* Pt. 1, pp. 92–93. The net income reported on individual income-tax returns (including those of fiduciaries) was 67 billion dollars, or roughly 57 per cent of income payments. Of this total, personal exemptions and credits for dependents accounted for 29.5 billions, leaving a surtax base of about 37.5 billions. Because of earned income credits allowed in 1942, taxable income subject to the normal tax was only about 31.7 billions.

[10] *Individual Income Tax Reduction,* Hearings before the Committee on Ways and Means, 80 Cong. 1 sess., p. 28. Earlier estimates by the Treasury Department indicated taxable income of 43.5 billions and a ratio of 33.5 per cent, with income payments at 130 billions. *Revenue Act of 1945,* Hearings before the Senate Committee on Finance, 79 Cong. 1 sess., p. 47. Estimates by the Committee for Economic Development indicate a postwar ratio of 42.5 per cent, with the national income at 140 billions and income payments at 135.2 billions. *A Postwar Federal Tax Program for High Employment* (1944), p. 43.

[11] Since recent Treasury estimates are based on a ratio of slightly less than 42 per cent with income payments at 166 billions, this figure may seem optimistic. With continued efforts to reduce the volume of taxable income escaping taxation, there will be some tendency for the ratio to rise.

total taxable income of 70 billions.[12] In order to obtain 12.4 billions of revenues, this income would have to be taxed at an average rate of 17.7 per cent. This is the flat rate that would be necessary if the personal income tax were a proportional tax rather than one imposed at progressive rates.

A standard rate of something like 15 per cent[13] would be necessary for the personal income tax. This rate would represent a decline of over one fifth from the present first-bracket rate of 19 per cent.[14] On the other hand, 15 per cent is a very high figure compared with prewar years. It would be almost four times the rate applicable to the first $4,000 of taxable prewar income. On incomes for 1938, 1939, and 1940, the normal tax was only 4 per cent, and the first $4,000 of surtax net income was not subject to surtaxes.[15]

Recent developments suggest that low net incomes may be taxed at preferential rates. If there is one certainty in the present picture, it is that when further reductions in personal income taxes are approved, taxpayers with small incomes will receive relatively larger reductions than those with higher incomes. This might be done in either of two ways: (1) by providing a special rate or rates for taxpayers with taxable incomes of not more than specified amounts; or (2) by establishing a somewhat lower standard rate (or comparable deductions from computed taxes) for the first bracket of taxable income. In preparing our estimates, it has been assumed that the second method will be employed. Accordingly, a rate of

[12] The difference between 165 billions and 70 billions would be accounted for by deductions on taxable returns, personal exemptions, a large volume of income below exemptions, and income not reported or exempt from income tax.

[13] Under the form of rate schedule used in earlier years this would be the normal rate, with all surtaxes given as extra or additional rates. Because of the peculiar use of "normal" in connection with the corporate rates in recent years, among other reasons, "standard rate" seems preferable to "normal rate."

[14] The nominal rate is 20 per cent, but a credit of 5 per cent of computed taxes is allowed.

[15] On 1940 incomes there was an additional defense tax equal to approximately 10 per cent of the computed tax.

13 percent has been used for the first \$1,000 of taxable income.[16]

From a revenue standpoint, the standard rate is of prime importance. Thus a standard rate of 15 per cent, with a special rate of 13 per cent for the first \$1,000 of taxable income, imposed on a taxable income of 70 billions would produce revenues of 9.8 billions. The great importance of the lower taxable income brackets is also clearly indicated by the table on page 70. According to our estimates, the first two brackets of \$1,000 each would account for about 70 per cent of all taxable income reported on individual returns and over one half of all personal income taxes. A large proportion of all taxpayers report taxable incomes of not over \$2,000.[17]

The significance of the lower brackets—and taxpayers with small incomes—is enhanced, when one considers that they are by far the most stable element in the tax base. This follows from the fact that the income consists very largely of wages and salaries; dividends and capital gains which fluctuate widely are relatively unimportant. The fact that high incomes can fluctuate substantially and still exceed the first-bracket limits is also a major factor making for stability.[18]

If 9.8 billions should be obtained from the standard rate of 15 per cent, together with the special rate for the first \$1,000, the requirement for surtaxes—or rates in addition to the standard rate—becomes 2.6 billions. This figure represents approximately one fifth of the estimated revenues from personal income taxes. With exemptions at a low level and

[16] The system here envisaged is roughly comparable to that used for 1933 and earlier taxable years. Thus, for the taxable years 1932 and 1933 the normal rate on the first \$4,000 was 4 per cent, and the rate on all taxable net income above \$4,000 was 8 per cent.

[17] If all married taxpayers should be granted the privilege of dividing their income between husband and wife for tax purposes, the lower taxable income brackets would become of even greater relative importance. This privilege is now restricted to taxpayers in the community property states. In this connection, see U. S. Treasury Department, *The Tax Treatment of Family Income* (mimeo.), June 1947.

[18] Harold M. Groves, *Postwar Taxation and Economic Progress* (1946), p. 176. In Groves' opinion the only alternative to an adequate standard rate is irrational forms of taxation.

ESTIMATED TAXABLE NET INCOME AND PERSONAL INCOME TAXES BY INCOME BRACKETS, 1951 OR 1952 [a]

Taxable Net Income Bracket (In thousands of dollars)	Taxable Net Income [b]		Tax Rates (Per cent)			Total Taxes (In millions of dollars)
	Millions of Dollars	Per Cent of Total	Standard Tax	Surtax	Combined Rate	
0–1	35,350	50.5	13		13	4,596
1–2	13,650	19.5	15		15	2,047
2–4	6,580	9.40	15	2	17	1,119
4–6	2,569	3.67	15	4	19	488
6–8	1,736	2.48	15	6	21	365
8–10	1,281	1.83	15	8	23	295
10–12	987	1.41	15	10	25	247
12–14	791	1.13	15	12	27	214
14–16	651	.93	15	14	29	189
16–18	553	.79	15	16	31	171
18–20	469	.67	15	18	33	155
20–22	413	.59	15	20	35	145
22–26	602	.86	15	22	37	223
26–32	686	.98	15	24	39	268
32–38	497	.71	15	26	41	204
38–44	392	.56	15	28	43	169
44–50	322	.46	15	30	45	145
50–60	385	.55	15	32	47	181
60–70	294	.42	15	34	49	144
70–80	217	.31	15	36	51	111
80–90	203	.29	15	38	53	108
90–100	168	.24	15	40	55	92
100–150	378	.54	15	42	57	215
150–200	196	.28	15	44	59	116
Over 200	630	.90	15	46	61	384
Total	70,000	100.00				12,391

[a] Income taxes collected during the fiscal year 1952 would be based mainly on returns for the taxable year 1951. However, income taxes withheld would include taxes paid on account of income reported on both 1951 and 1952 returns.

[b] This distribution is based primarily on the distribution in *Individual Income Tax Reduction,* Hearings before the Committee on Ways and Means, 80 Cong., 1 sess., p. 29.

a high standard rate, a sharp change—compared with prewar years—in the distribution of total individual taxes between the standard tax and surtaxes is inevitable.

Raising 2.6 billions from the surtax schedule would require

dipping far down in the income scale. The brackets of taxable income subject only to the standard rate would have to be held within narrow limits, certainly no more than the first $2,000. Examination of the distribution of net income reported on returns for earlier years, together with the current estimates of the Treasury, indicates clearly that no other alternative is available if the required revenues are to be obtained. More or less complete abandonment of the idea that the income tax can retain the characteristics of a class tax would be necessary.

A distribution of taxable income and personal income taxes by income brackets is shown in the table on page 70.[19] This table should not be regarded as a forecast of the taxes that will be borne by the several income brackets. Rather, the object is merely to indicate the nature of the problem involved in raising over 12 billions from personal income taxes.

Second Approach

We next consider what would be involved if the rates for the corporate income tax should be reduced to a much lower level than was suggested by the preceding analysis. Specifically, it will be assumed that the place of the corporate income tax in the postwar tax structure will correspond with that proposed in an earlier study. Under the plan there suggested, the objective would be a reduction in the basic corporate tax rate from the wartime level of 40 per cent to a rate in the range of 5 to 10 per cent. This tax would be in the nature of a surtax or special tax; in addition, the standard rate would be collected on corporate income at the source.[20]

Corporate income tax. Under this approach, the rate for the corporate tax might be 8 per cent. If the tax base should be 20 billions, a rate of 8 per cent would yield revenues of 1.6

[19] The total amount distributed in this table is slightly less than 12.4 billions.

[20] Lewis H. Kimmel, *Postwar Tax Policy and Business Expansion* (1943), pp. 12 ff.

billions.[21] This figure is less than one third of the estimate under the first approach.

Standard tax collectible at source. Since the standard rate for the income tax would be collected at the source, the additional amount collectible from corporations on account of this rate will be considered at this point. With 3.4 billions less obtained from the corporate tax than under the first approach, a standard rate of perhaps 17 per cent for the income tax proper would be required. At this rate an additional amount of about 3,130 millions would be collected directly on corporate profits.[22]

If one third of the net profits of 18.4 billions after payment of the special corporate tax should be retained, one third of the standard tax or roughly 1,040 millions would be chargeable to retained earnings. This part of the tax would be in the nature of an undistributed profits tax. The other two thirds would properly be regarded as withheld taxes and would be claimed by recipients of dividends[23] as credits against their computed taxes.[24]

Personal or individual income tax. With total income taxes at 17.4 billions, the amount to be derived from taxes on indi-

[21] It will be observed that we have used the same estimates for profits as under the first approach. To the extent that the corporate income tax has been shifted, a substantially lower rate would tend to bring about lower profits before taxes. Though there might be some justification for reducing profits before taxes on the assumption that part of the tax has been shifted, such a procedure would be decidedly arbitrary. There is no reason to believe that adjustment to the changed situation would be completed during the fairly short period with which we are here concerned.

[22] This estimate assumes that the base to which this rate applies would be 18.4 billions or total profits less the special corporate tax of 8 per cent. If the corporate tax were imposed as a business tax, deduction of this tax in arriving at the base for the standard tax would represent the only logical procedure. Indeed, deduction of the special corporate tax before computing the standard tax would be essential if the allocation of the latter tax to dividends and undistributed earnings were to be effected on the basis of the standard rate.

[23] No allowance is here made on account of dividends received by corporations or by those with incomes so low that an income tax is not required.

[24] Under this plan dividends would be declared on a basis that includes the standard tax, and net dividends would equal gross dividends less this tax. Gross dividends would be reported for individual income taxes, and appropriate credit would be taken for the taxes withheld at the source.

vidual incomes[25] becomes about 14.8 billions. This figure is obtained as follows:

	(Millions of dollars)	
Total income taxes..................		17,400
Less: Corporate tax..................	1,600	
Standard tax on retained earnings	1,040	2,640
Personal income tax............		14,760

On the basis of taxable income of 70 billions,[26] the same amount as under our first approach, an average rate of 21.1 per cent would be required. Under this approach a standard rate of 17 per cent might be imposed, with the rate for the first $1,000 also 2 percentage points above that in the table on page 70. In this event, the standard rate (including the special rate of 15 percent for the first $1,000) would yield about 11.2 billions.[27] The remainder of roughly 3.6 billions would be obtained from the surtax schedule, or rates in addition to the standard rate.

The distribution of the total income-tax requirement under the second approach is shown in the following tabulation:

	(Millions of dollars)	
Corporate income tax at 8 per cent.....		1,600
Standard tax of 17 per cent on retained corporate earnings		1,040
Taxes on personal incomes:		
Standard tax withheld at source on dividends	2,090	
Standard tax on all other income....	9,110	11,200
Surtaxes on personal incomes........		3,560
Total income taxes........		17,400

[25] Income payments to individuals would include all withheld personal income taxes on dividends as well as on wages and salaries.

[26] It is recognized that taxable income might be somewhat larger than this figure, because of the changed situation with respect to the corporate income tax. However, assuming no reductions in prices by reason of the lower corporate tax, the maximum increase in taxable income would probably not be much over 1 billion dollars.

[27] Of this amount, 2,090 millions would be withheld from dividends and paid directly to the Treasury.

II. ESTATE AND GIFT TAXES

The 1952 estimate for estate and gift taxes under the revenue program on p. 64 is 975 millions. This figure is over two and one half times the yield for 1940.

Revenues from estate and gift taxes have shown a marked upward trend in recent years. For the fiscal year 1947 the yield was 779 millions, an increase of more than 100 millions over 1946. Collections for 1944 were 511 millions, and for 1945 they were 643 millions. In 1940 only 360 millions was obtained from these taxes.

The present upward trend in revenues from these taxes is mainly a result of three factors. First, there is the higher level of values; adjustment to the new level, however, will doubtless be very gradual. Second, the enormous rise in holdings of government securities and liquid savings during the war years has tended to bring about an increase in the dollar value of decedents' estates. A third factor is the trend towards more effective administration, especially the closing of various means of escape.[28]

III. LIQUOR AND TOBACCO TAXES

The liquor and tobacco taxes have long been the most productive federal excises. Originally, these commodities were selected as tax objects because their consumption was widely regarded as harmful. While the sumptuary argument is still advanced in justification of the high rates imposed, the revenues derived are the paramount consideration.

Liquor taxes. Under the revenue program in the table on page 64, liquor taxes would amount to about 2 billions for 1952. This figure is more than three times 1940 revenues.

[28] With this factor—among others—in mind, Roswell Magill included 1 billion dollars for estate and gift taxes in his postwar estimates prepared in 1943. *The Impact of Federal Taxes* (1943), p. 41.

The integration of the federal estate and gift taxes has been recently proposed. See *Federal Estate and Gift Taxes* (1947). This is a joint study prepared by the Treasury Department's Advisory Committee on Estate and Gift Taxation and the Office of the Tax Legislative Counsel, with the co-operation of the Division of Tax Research and the Bureau of Internal Revenue.

As a result of increases in rates and high consumption, revenues rose sharply during the war years. Between 1940 and 1943 revenues more than doubled. For 1943 the total was slightly over 1.4 billions, while for 1945 it was 2.3 billions. The corresponding total for 1946 was over 2.5 billions, and that for 1947 was slightly under this figure.

The figure of 2 billions assumes that the special war rates effective April 1, 1944 will be continued through the fiscal year 1952. The Revenue Act of 1943 provided for increases from $6 to $9 per proof gallon of distilled spirits, and from $7 to $8 per barrel of fermented malt liquors. The increase for most wines was equivalent to 50 per cent. The 1943 act provided that these rates should remain in effect for six months (or slightly more) after the end of hostilities was officially proclaimed. Under more recent legislation, however, they will be continued indefinitely.[29]

On the other hand, consumption may run well below the recent peak. During the war and immediate postwar years consumption was probably abnormal in some respects. At any rate, this is strongly suggested by the sharp decline in retail sales in the first half of the calendar year 1947, a period of substantially full employment and high incomes. As a consequence of this decline, federal collections dropped sharply. For the April-June quarter, they were only 479 millions, as compared with 627 millions for the same quarter of 1946.[30]

Tobacco taxes. The 1952 revenues from the federal tobacco excises shown in the table on page 64 are 1.4 billions, or more than double the 1940 total.

During the war years revenues from the tobacco taxes mounted rapidly. Compared with the 1940 total of 608 millions, revenues for 1944 were 989 millions. A slight decline

[29] Public Law 17, 80 Cong. 1 sess.

[30] The sharp decline in sales and consumption at a time when incomes have been unusually high raises a question whether combined federal and state tax rates may not in many cases have risen beyond the point of diminishing returns. Another possibility is that the decline in war-period tensions has contributed to reduced consumption. Perhaps both factors are of some significance.

in the following year was attributable to the cigarette shortage in the spring and early summer of 1945. In 1946 revenues amounted to about 1,166 millions, and for 1947 they were 1,238 millions.

There have been two main reasons for the sharp increase in revenues. First, consumption—especially of cigarettes—increased enormously under wartime conditions. Second, the rate on standard-sized cigarettes was increased from \$3.25 to \$3.50 per 1,000 by the Revenue Act of 1942. The tax on standard-sized cigarettes[31] produced over 92 per cent of all revenues from tobacco taxes in the fiscal year 1947.

IV. MANUFACTURERS' AND RETAILERS' EXCISES

There are two sharply divergent points of view with respect to the role of the federal manufacturers' and retailers' excises. According to one school of thought, these taxes—with the possible exception of the gasoline tax—should be repealed. Those favoring this course stress the fact that these taxes represent heavy burdens on consumption. Most taxes based on sales, it is claimed, should be discontinued in the interest of maintaining high-level consumption. Exception would be made only for taxes on liquor and tobacco—and perhaps gasoline.

The opposing view emphasizes that a broad group of federal excises is desirable—for two reasons. First, it is said that the large revenue needs of the postwar years will make it impracticable to rely almost exclusively on income taxes, together with the estate and gift taxes and the liquor and tobacco taxes. Second, it is argued that well-chosen taxes on sales or consumption contribute to revenue stability, since under adverse economic conditions sales do not decline as rapidly as net income.

[31] Technically, there is no such thing as a standard-sized cigarette. For tax purposes cigarettes are classified between those weighing no more than 3 pounds per thousand and those weighing more than 3 pounds per thousand. That the larger cigarettes are of almost negligible importance is indicated by the fact that revenues for 1947 amounted to less than \$6,300, as compared with 1,145 millions for small cigarettes.

Recent developments suggest that the second point of view is likely to prevail. Faced with revenue requirements that are enormous by earlier peacetime standards, it does not appear likely that the Congress will eliminate many of the most productive excises and reduce others to the barest minimum. The fact that reliance has been placed on manufacturers' excises for a substantial volume of revenues continuously since 1932 re-enforces this view.

Manufacturers' excises. This excise group includes taxes on gasoline, lubricating oils, automobiles and trucks, automobile parts and accessories, tires and inner tubes, mechanical refrigerators, radio receiving sets, and electrical energy, together with other minor commodities. Under the revenue program in the table on page 64, the yield of these taxes is placed at 1,650 millions for 1952.

Manufacturers' excises have shown a sharp upward trend. Revenues for 1940 were 447 millions. The comparable totals for 1945 and 1946 were 783 millions and 923 millions, while that for 1947 was 1,425 millions. Although revenues from taxes on automobiles and trucks and other consumers' durables declined precipitately during the war years, 1945 collections for the entire group of taxes were roughly 75 per cent above those for 1940. Rate increases were primarily responsible for this upward trend. The sharp rise in 1946 and 1947 was accounted for mainly by the mounting yields of the automotive excises following the restoration of peacetime production.

Retailers' excises. Sales of furs, jewelry, toilet preparations, and luggage are subject to federal excises at the retail level. These taxes were primarily a development of the war years. No levies in this category were imposed in 1940, but there was a manufacturers' tax on toilet preparations.[32]

From the modest total of 80 millions for 1942, revenues increased sharply, reaching a peak of 514 millions for 1947. Rate increases enacted in 1943 contributed importantly to the rising yield. Under the provisions of the act continuing special

[32] The 1940 yield of this tax was less than 8 millions.

wartime rates for excises, these taxes are continued indefinitely at the wartime rates. There is reason to believe, however, that the rates for some of these taxes will soon be reduced or the form of taxation changed. Accordingly, only 300 millions has been included for 1952 for this group of taxes.

V. OTHER INTERNAL REVENUE TAXES

Under this heading we consider: (1) miscellaneous excises; (2) stamp taxes; and (3) the unemployment tax.

Miscellaneous excises. The principal taxes in this group are those on transportation of persons and property, admissions, and communications. Other taxes of lesser revenue importance include those on club dues and initiation fees, transportation of oil by pipe line, coin-operated devices, and the special tax imposed under the Sugar Acts of 1937 and 1948.

Revenues increased enormously during the war years, mainly as a result of the addition of new tax objects and higher rates. From a total of 157 millions for 1940, revenues rose to more than 1.4 billions by 1945. In the following year collections were almost 1.5 billions, and for 1947 the yield was 1,551 millions. Despite the repeal of the automobile use tax which produced 116 millions in 1946, revenues for 1947 showed a gain of 61 millions.

The future of some of these taxes is surrounded with considerable uncertainty. In particular, there is a possibility that the taxes on transportation—especially of property—will be repealed or modified before 1952. Taking into account the several contingencies, we have included revenues from miscellaneous excises in the amount of 850 millions for 1952 in the table on page 64.

Stamp taxes. Federal levies classed as stamp taxes include the documentary stamp taxes on deeds, bonds, and the like, the transfer of capital stock or similar interest, the playing-card tax, and the tax on sales or transfers of silver bullion. These taxes are only of minor revenue importance. For 1940 the aggregate yield was 39 millions; comparable totals for 1946 and 1947 were 88 millions and 80 millions. Under the

1952 program here outlined, revenues from stamp taxes would amount to 85 millions.

Unemployment tax. The tax here considered is the pay-roll or employment tax imposed for unemployment compensation purposes on the employers of eight or more persons. The nominal rate is 3 per cent, but since a credit up to 90 per cent of the tax can be claimed for taxes paid to the states, actual federal collections are not much more than one tenth of those collectible at the full rate.[33] This tax differs from the old-age tax in that the moneys derived are treated as general revenues; they are not transferred to a trust account. Although a substantial portion of the yield is in effect offset by appropriations to the states for the administration of unemployment compensation, the revenues are not specifically earmarked for this purpose.[34]

In common with other pay-roll taxes, revenues increased rapidly during the war years. From 106 millions for 1940, receipts rose to 183 millions for 1944 and 186 millions for 1945. For 1946 the yield was 179 millions and for 1947 it was 186 millions. Revenues for 1952 may amount to 190 millions.

VI. CUSTOMS DUTIES

Prior to the war customs revenues were at a low level. The net yield for 1940 was only 332 millions. Only minor changes occurred during the war years; revenues for 1945 were less than 350 millions. After 1945, however, revenues rose sharply. The yield was roughly 425 millions for 1946 and about 475 millions for 1947.

[33] See Chap. 7, p. 125.

[34] Revenues from this tax and administrative costs have been linked together from the beginning of the social security system. See, for example, the statement by Frances Perkins in *Economic Security Act,* Hearings before the Senate Committee on Finance, 74 Cong. 1 sess., p. 112. More recently, the social security technical staff of the Ways and Means Committee wrote: "The source of funds for congressional appropriations for grants to States is generally considered to be the Federal unemployment tax collected by the Federal Government, which amounts generally to 0.3 per cent of the taxable wages paid by employers subject to it." *Issues in Social Security* (1946), p. 365.

Customs revenues in the years ahead will depend on a number of factors, including the extent of economic recovery in Europe and the degree of success attained by the efforts to stimulate international trade. Under the revenue program on page 64, a yield of 550 millions would be obtained from this source in 1952.

VII. NONTAX RECEIPTS

In popular discussion taxes and revenues are frequently regarded as identical. Though taxes account for by far the largest portion of federal revenues, there are other sources. Nontax revenues and miscellaneous receipts of the federal government include proceeds from the sale of government products, property and services, reimbursements, repayments of investments, mint receipts, and a wide variety of minor items.

Federal miscellaneous receipts are currently at abnormal levels. The total—general and special accounts—amounted to over 4.8 billions for the fiscal year 1947, as compared with about 3.5 billions for 1946. The budget estimate for 1948 is 4.4 billions, and that for 1949 is 2.3 billions. The sharp decrease for 1949 is accounted for in part by the decline in receipts from the sale of government property and products.[35]

Miscellaneous receipts of 640 millions for 1952 are included in the table on page 64. A breakdown by principal classifications is shown in the table on page 81. In 1952 miscellaneous receipts may still be influenced to some extent by the aftermath of the war. However, after the liquidation of World War II has been fully completed, the annual total will probably not differ materially from the 1952 estimate.

Sales of government products. Receipts from the sale of government products are placed at 200 millions for 1952, or

[35] The estimates in this paragraph are on a higher basis than our figure for 1952. Included in these totals are numerous transfers from government corporations to the Treasury on account of interest and repayment of principal. In the present study the finances of government corporations and credit agencies are included on a net basis only; that is, receipts are balanced against expenditures and only the excess of expenditures over receipts is considered a general revenue requirement.

about one sixth of the official estimate for 1948. According to the budget estimates, there will be a sharp decline from a peak of almost 2.5 billions to 1.4 billions for 1948 and about 575 millions for 1949. As sales of surplus property[30] in the United States and in foreign countries currently account for the bulk of the income, further sharp decreases can be expected in later years. One of the largest nonwar items in this classification is receipts from the sale of scrap and salvaged materials, condemned stores, waste paper, refuse, and the like.

ESTIMATED FEDERAL RECEIPTS FROM MISCELLANEOUS NONTAX SOURCES, FISCAL YEAR 1952
(Millions of dollars)

Source	Estimated Receipts
Sales of government products	200
Sales of government property	50
Sales of services	25
Reimbursements	100
Repayment of investments	50
Mint receipts	65
All other	150
Total	640

Sales of government property. Currently the principal items in this classification are proceeds from the sale of surplus vessels and receipts from surplus property in foreign areas. We have included 50 millions from this source for 1952.

Sales of services. Receipts from sales of services are included in the amount of 25 millions. This figure excludes the Panama Canal tolls and receipts credited to the Alaska Railroad fund. Both agencies are classed under "governmental business enterprises" in this study.

Reimbursements. Receipts on account of reimbursements are placed at 100 millions for 1952. The estimate for 1948 is 512 millions. In recent years excessive profits on renegotiated contracts recovered by the government have accounted

[30] Curiously, most of the receipts from the sale of war surpluses are being covered into the Treasury under "sales of government products" rather than sales of government property.

for the major portion of receipts included in this classification. The official estimate for 1948 is 196 millions, as compared with almost 1.1 billions for 1946. As renegotiation proceeds decline, total receipts from reimbursements will dwindle to a much lower level.

Repayment of investments. The figure of 50 millions for receipts in this classification includes payments from the public to the Treasury. The principal items are repayments on rural rehabilitation loans and on crop production and harvesting loans. Repayments of principal by government corporations to the Treasury are excluded.

Mint receipts. Profits are derived from some of the operations of the United States mints. Seigniorage accounts for the bulk of these profits. This profit results from the difference between the cost of the metal used—especially silver—and the face value of the minted coins. Though seigniorage is not strictly a receipt from the public, the net effect of such receipts is to offset a like amount of cash expenditures in the over-all accounts. Mint receipts amounted to 62 millions for 1947. We have included 65 millions for 1952.

Other receipts. Miscellaneous receipts from all other sources are placed at 150 millions. Included are rents and royalties, interest, fees, fines and forfeitures, and assessments, among other items.

CHAPTER V

STATE TAXES AND OTHER REVENUES

The analysis in Chapter II indicated state expenditures of roughly 6.1 billions for 1952. Assuming these expenditures are to be covered by current revenues,[1] the pattern of taxes would be something like that presented in the table on page 84. Revenues for 1940 and 1946 are included for comparison.

In developing the estimates in this chapter, we have assumed that no major new types of state taxes will be adopted between 1947 and 1952. Major consideration has been given to the form of state tax systems and the level of the national income.

I. SALES, USE, AND GROSS RECEIPTS TAXES

Under the revenue plan in the table on page 84, revenues from sales, use, and gross receipts taxes would amount to 1.3 billions for 1952.[2] In arriving at this figure, we have first considered the level of revenues for the 23 states which levied taxes of the retail or general type in 1946. Adjustment was then made for the four states which adopted sales taxes in 1947.[3] As a last step, account was taken of possible additions and increases in rates between 1947 and 1952.

[1] The balance between revenues and expenditures here assumed is of course merely a convenient working assumption. A portion of state revenues will be used to retire state debts. On the other hand, certain expenditures —especially capital outlays—will be covered from borrowed funds. Moreover, because of revenues set aside and balances accumulated during the war years, the states may find it unnecessary to raise revenues equal to the full amount of their expenditures. However, for our purpose it would not be desirable to make an arbitrary adjustment. Our principal concern is with the level of revenue needs; the reserve funds and cash balances referred to are only of short-run significance.

[2] The several taxes are discussed on the basis of total yields; deduction on account of local shares is made from the combined total for state tax collections. See the table on p. 84.

[3] The four adoptions in 1947 (Connecticut, Maryland, Tennessee, and Rhode Island) represented the first additions to the sales tax states in a decade. The sales tax movement of the 1930's was primarily a depression phenomenon. See Roy G. and Gladys C. Blakey, *Sales Taxes and Other Excises* (1945), p. 2.

STATE TAXES AND OTHER REVENUES, ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940 AND 1946
(In millions of dollars)

Source	1940 [a]	1946 [a]	1952
Taxes:			
General sales, use, and gross receipts taxes	499	900	1,300
Corporate income tax	155	442	450
Personal income tax	206	389	450
Death and gift taxes	113	146	185
Liquor taxes	255	469	400
Tobacco taxes	97	199	400
Property taxes	260	253	210
Severance taxes	53	90	90
Miscellaneous taxes	449	744	825
Motor vehicle fuel taxes	839	887	1,325
Motor vehicle licenses [b]	387	461	600
Total taxes	3,313	4,980	6,235
Local shares	271	325 [c]	450
Net state taxes	3,042	4,655	5,785
Nontaxes:			
Charges for current services	195	240 [c]	250
Miscellaneous	44	50 [c]	50
Total nontaxes	239	290 [c]	300
Total revenues	3,281	4,945	6,085

[a] Data for 1940 from U. S. Bureau of the Census, *Financial Statistics of States: 1940*, Vol. 3; data for 1946 from the Bureau's *State Tax Collections in 1947* and other releases.
[b] Includes operators' licenses.
[c] Estimated.

In 1940 the states collected 499 millions in sales taxes. As a result of wartime prosperity, the total rose sharply in later years. By 1944 collections amounted to 721 millions, and for 1945 they were 776 millions. The 1946 yield was 900 millions; the preliminary figure for 1947 is 1,179 millions.[4] These increases were achieved despite the dearth of durable consumers' goods during the war years[5] and short supplies in some lines in the first two postwar years.

[4] Unless otherwise indicated, all data for completed fiscal years in this chapter are from the U. S. Bureau of the Census, *Financial Statistics of States* series; the preliminary figures for 1947 are from the Bureau's *State Tax Collections in 1947*, August 1947.

[5] From 1942 to the end of hostilities sales of consumers' durables were well below the level of 1940–41; annual sales were roughly the same as for 1938.

As a first step in obtaining the 1952 estimates, retail sales for 1939 to 1946 were compared with income payments and disposable income. These comparisons are shown in the table below. In the immediate prewar years the ratio of retail sales to income payments was almost exactly 60 per cent.[6] On the other hand, this ratio declined sharply during the war years, reaching a low of about 44 per cent for 1944. However, immediately after the end of hostilities insistent demands for consumers' goods soon brought the ratio to a figure comparable to those for the immediate prewar years. Considering the uneven situation in consumers' goods lines and the high direct taxes which prevailed, the recovery was extraordinarily rapid.

RETAIL SALES COMPARED WITH INCOME PAYMENTS AND DISPOSABLE INCOME, CALENDAR YEARS 1939–46 [a]

Year	Retail Sales (In billions of dollars)	Income Payments (In billions of dollars)	Disposable Income (In billions of dollars)	Ratio of Retail Sales to	
				Income Payments (Per cent)	Disposable Income (Per cent)
1939	42.0	70.8	67.7	59.3	62.0
1940	46.4	76.2	72.9	60.9	63.6
1941	55.5	92.7	88.7	59.9	62.6
1942	57.6	117.3	110.6	49.1	52.1
1943	63.7	143.1	124.6	44.5	51.1
1944	69.5	156.8	137.4	44.3	50.6
1945	76.6	160.8	139.6	47.6	54.9
1946	96.7	165.1	146.0	58.6	66.2

[a] Data from U. S. Department of Commerce, *Survey of Current Business.*

In a period characterized by marked changes in direct taxes,[7] disposable income is a better comparative for retail

[6] The average for 1939, 1940, and 1941 was only fractionally above this figure.

[7] For the calendar year 1946 combined federal, state, and local personal tax and nontax payments were 19.1 billions, as compared with 3.3 billions for 1940. U. S. Department of Commerce, *Survey of Current Business,* February 1947, p. 7 and April 1944, p. 14.

sales than income payments. Before World War II retail sales amounted to about 62 per cent of disposable income. The low for the war years was roughly 50 per cent for 1944; because of shortages, rationing, and wartime inducements to save, a sharp decline was inevitable. On the other hand, in 1946 retail sales amounted to almost two thirds of disposable income, a ratio somewhat higher than those for the immediate prewar years.

A high ratio of retail sales to disposable income seems likely for 1952. With national income at 175 billions and income payments at 165 billions, disposable income would no doubt be roughly 150 billions.[8] At this level the ratio of retail sales to disposable income would probably be as high or slightly higher than that for 1946. The range is placed at 65 to 70 per cent, with 66.7 per cent the most likely expectation. On this basis, retail sales would fall somewhere between 97.5 billions and 105 billions, with 100 billions the probable figure.

Our next step is to consider the relation between sales tax receipts and retail sales.[9] From 1939 to 1946, state sales tax revenues ranged between 1.06 per cent and 1.14 per cent of all retail sales in the United States, as shown in the table on page 87. The stability of the ratio was mainly a result of the fact that the same states imposed this type of tax during the entire period. Even greater stability would doubtless have prevailed, if the Illinois rate had not been reduced from 3 per cent to 2 per cent as of July 1, 1941.

The sales tax revenues of the 23 states imposing sales taxes in 1946 at the rates then in effect should amount to somewhat more than 1 per cent of estimated retail sales for the nation.

[8] The difference between the figures for income payments and disposable income is accounted for by federal personal income taxes, certain state and local taxes, and nontax payments.

[9] Taxes on retail sales plus the complementary use taxes account for all but a small portion of state sales tax revenues. In 18 of the 23 states using sales taxes in 1946, the tax is of the retail type. The present figure is 22 out of 27. In the five states in which general sales or gross receipts taxes are imposed, the rate on retail sales usually produces the bulk of the revenues.

For the purpose of our estimates, the ratio is placed at 1.1 per cent. Using the figure for retail sales previously derived, the revenues for the 23 states become 1,100 millions.

Four states, as previously noted, enacted sales tax laws in 1947.[10] The Connecticut sales and use taxes, which are imposed at the rate of 3 per cent, will probably yield something

State Sales Taxes Compared With Retail Sales, Fiscal Years 1939–46

Year	State Sales Taxes[a] (In millions of dollars)	Retail Sales[b] (In billions of dollars)	Ratio of State Sales Taxes to Retail Sales (Per cent)
1939	440	39.8	1.11
1940	499	44.2	1.13
1941	575	50.4	1.14
1942	633	56.5	1.12
1943	671	60.4	1.11
1944	721	66.3	1.09
1945	776	71.5	1.09
1946	900	84.6	1.06

[a] Data for fiscal years ended in years indicated from U. S. Bureau of the Census, *Financial Statistics of States* series. The fiscal years of 18 of the 23 states imposing sales taxes in 1946 end on June 30.
[b] Data for years ended June 30 computed from monthly figures in U. S. Department of Commerce, *Survey of Current Business.*

like 45 millions for 1952.[11] For the purpose of our estimates, the yield of the Maryland tax will be placed at 20 millions,[12]

[10] Five state legislatures approved sales tax laws in 1947. The Oregon tax was rejected by the electorate in a referendum vote held Oct. 7, 1947.

[11] This figure is substantially higher than the estimate of 26 millions used when the bill was under discussion. Investigations by the State Tax Department suggest that at a high level of national income a yield of as much as 52 millions might be obtained; letter dated July 24, 1947. Revenues for the first quarter were about 9.6 millions. *New York Times,* Oct. 29, 1947, p. 29.

[12] At the time of enactment in March 1947, the yield of the Maryland sales tax was estimated at 18.4 millions. On the basis of collections for the first two months, collections for the first year have been estimated by the State Controller at 25 millions. *The Evening Star* (Washington), Sept. 26, 1947, p. B-1.

and that of the Rhode Island tax at 6 millions.[13] The new Tennessee tax will probably produce annual revenues of something like 35 millions.[14] In addition to these four new taxes, minor changes were made in the sales tax bases in Iowa[15] and Kansas, among other states. Adding 4 millions for these changes, the combined adjustment on account of 1947 adoptions and changes becomes 110 millions. On the basis of the present situation, revenues of 1,210 millions might reasonably be expected for 1952.

The final step is to take into account the probable developments in state sales taxation between 1947 and 1952. According to present indications, a sales tax may soon be considered in Pennsylvania and other states. In order to allow for new adoptions, rate changes, and adjustments in tax bases, we have increased the total from 1,210 millions to 1,300 millions.

II. INCOME TAXES

Taxes based on net income are currently imposed by approximately 35 states.[16] In common with the sales tax movement, the development of state income taxes is fairly recent. Only 15 states imposed income taxes before 1928, but six states adopted this form of tax in 1929. A large number of adoptions during the 1930's, particularly in the first half of the decade, brought the total to the present level.[17]

Corporate income taxes. The taxes on corporate income are imposed by the same states which tax individual incomes—with a few exceptions. In Pennsylvania there is only a cor-

[13] The yield has been placed at 6.2 millions. *Tax Administrators News,* June 1947, p. 65.

[14] The yield of Tennessee's 2 per cent sales and use taxes, which became effective June 1, 1947, has been placed at 20 millions to 45 millions annually. *Tax Administrators News,* Vol. 11, February 1947, p. 17.

[15] The Iowa legislature meeting in 1947 imposed a 2 per cent tax on commercial amusements, extending the sales tax to include pool and billiard halls, slot machines, juke boxes, shooting galleries, and the like. Letter from State Tax Commission, Apr. 19, 1947.

[16] The exact number depends on whether taxes of limited application such as those in New Hampshire and Tennessee are included.

[17] Roy G. Blakey and Violet Johnson, *State Income Taxes* (1942), pp. 3–4. It should not be inferred that a completely stationary situation developed.

porate income tax; the personal income tax originally enacted was declared unconstitutional. Tennessee also imposes a tax on corporate income, but only income from intangibles is taxable to individuals.

State revenues from corporate income taxes increased rapidly during the war years. From 1940 to 1943 collections more than doubled; the totals for these two years were 155 millions and 340 millions. A further increase of over 100 millions was reported for 1944 and for the following year the total was 453 millions. The comparable yield for 1946 was 442 millions; the preliminary figure for 1947 is 461 millions. The marked rise in revenues during the war years was a direct result of the enormous expansion of business profits. Revenues were not much affected by changes in rates which were generally continued at prewar levels.[18]

In the absence of rate increases and new adoptions, revenues from state corporate income taxes would tend to decline to the extent that there is a compression of business profits. An offsetting factor, however, is that roughly two thirds of the states levying corporate income taxes permit the deduction of federal income or profits taxes. In these states discontinuance of the excess profits tax as of the end of 1945, together with moderate reductions in federal corporate income-tax rates, has meant considerable support for state tax bases.[19]

[18] It should not be assumed that no changes were made. In 1946 New York reduced the rate on corporations from 6 per cent to 4.5 per cent and that on unincorporated businesses from 4 to 3 per cent. *Session Laws* (1946), Chap. 110. These changes did not affect collections during the year ended Mar. 31, 1946. In Pennsylvania the rate was reduced from 7 per cent to 4 per cent effective for the taxable year 1943; at the same time the deduction for federal income and profits taxes was eliminated. No decline in revenues occurred as a result of the latter change; collections for the year ending May 31, 1944 were actually about one-third larger than those for the preceding year.

[19] A word of caution is necessary, lest the statement that two thirds of the income tax states permit deduction of federal income taxes paid or payable leave an exaggerated impression of the significance of the changes at the federal level. Federal taxes are not deductible in New York, California, and Pennsylvania. These three states together accounted for about 62 per cent of state corporate income taxes in 1946; New York alone accounted for 40 per cent of the total.

It will be here assumed that roughly one half of total state corporate income taxes collected in 1952 will be based on net profits before federal income taxes and that the other half will be based on net profits after federal income taxes. On this basis, the "nation-wide" state corporate income-tax base corresponding to net profits of 20 billions before federal income taxes would perhaps be about 17.5 billions.[20] Since the comparable average for the years 1943, 1944, and 1945, on which state taxes collected in the fiscal years 1945 and 1946 were mainly based, was close to 17 billions, a level of collections comparable to that for 1945 and 1946 is indicated—say 440 millions or 450 millions. As previously mentioned, however, this level of revenues could reasonably be expected only if rates remain unchanged.

Our next step is to take account of rate changes. Though the New York rate may remain at 4.5 per cent for several years, there is a possibility that the 6 per cent rate will be restored before 1951.[21] Accordingly, we shall make no adjustment on account of the New York rate change.[22] Rate adjustments in other states approved in 1947 will probably mean a small rise in revenues. The effect of the lower rate in Oklahoma is doubtless more than offset by rate increases in Maryland, Vermont, and Colorado.[23] Taking into account these changes, we have included 450 millions for corporate income taxes in the table on page 84.

Personal income taxes. Under the influence of wartime

[20] This figure is the average of 20 billions for net profits before the federal income tax and 15 billions for net profits after this tax.

[21] The decline from 1946 to 1948 in receipts from the New York franchise tax (Art. 9a) is officially estimated at 47 millions. However, this decline is offset in part by an increase of 8 millions for the bank tax, which is also measured by net income. *New York Times,* Feb. 2, 1947, sec. 1, p. 48.

[22] As mentioned in footnote 18, p. 89, collections in New York for the fiscal year 1946 were not affected by the reduction in rate to 4.5 per cent. Accordingly, adjustment would have to be made only if a rate of less than 6 per cent was assumed for the early 1950's.

[23] *Tax Administrators News,* Vol. 11, February 1947, p. 16; April 1947, p. 43; May 1947, p. 55; and June 1947, p. 67. No further adjustment is made to take account of other changes between 1947 and 1952.

prosperity, collections on account of personal income taxes rose from 206 millions for 1940 to 357 millions for 1945. The comparable yield for 1946 was 389 millions; the preliminary figure for 1947 is 418 millions.

The marked increase in collections during the war years was achieved despite repeal of personal income taxes by two states and reductions in rates in other states. The over-all statistical picture was not much affected by the repeal of the West Virginia and South Dakota taxes;[24] these two states together accounted for less than 1 per cent of state personal income taxes for 1940. On the other hand, certain reductions in rates materially affected the level of collections.

Rate reductions in New York tended to slow down the upward trend in combined state income tax revenues.[25] The emergency income tax of 1 per cent—first enacted in 1932—was omitted for 1941 income taxes payable in 1942 and has not since been reimposed. In addition, a 25 per cent reduction for taxes computed at the regular personal income-tax rates was made effective for 1941 taxes payable in 1942.[26] This reduction was continued in effect for taxes on incomes for 1942–44.[27] The reduction was increased to 50 per cent for taxes for the calendar year 1945 payable in 1946.[28]

Significant changes were also made by other states. For example, Iowa granted a credit of 50 per cent of computed taxes with respect to taxes on incomes for 1942–45 payable in the following years.[29] In sharp contrast with the reduc-

[24] George H. Watson, "State Tax Legislation—1943," National Tax Association, *Proceedings* (1943), p. 7.

[25] New York accounted for slightly over one half of all state personal income taxes collected in the United States in 1940. The comparable proportion for 1946 was 38 per cent.

[26] Beulah B. Thull, "1942 State Tax Legislation," National Tax Association, *Proceedings* (1942), p. 40.

[27] Discontinuance of the emergency tax and the 25 per cent reduction were equivalent to a cut of 50 per cent for the lower income brackets.

[28] New York Session Laws (1946), Chap. 109. The reference here is to 1945 taxes payable Apr. 15, 1946 or thereafter. Since the fiscal year of New York ends March 31, this change did not affect collections for the fiscal year ended Mar. 31, 1946.

[29] Iowa *Acts,* 50 G.A. (1943), Chaps. 195–96 and 51 G.A. (1945), Chap. 44. The 1947 legislature authorized continuance of the "half-rate basis"

tions in New York, this step affected the total for all state individual income taxes by something like 2 per cent. Other changes such as discontinuance of the Wisconsin surtax for teachers' retirement and rate reductions in Mississippi also affected the level of collections for all states combined.

In our approximations for 1952, we shall first consider the level of revenues at the rates and exemptions which prevailed with respect to 1946 collections. State income taxes collected in the fiscal year 1946 were based mainly on incomes for 1944 and 1945. In these years annual income payments amounted to roughly 160 billions. At this level the yield of state personal income taxes, as we have seen, was 389 millions. If income payments on which 1952 collections are based should be 165 billions, a more than proportionate increase in collections could reasonably be expected, especially in the states permitting deduction of the federal tax. Federal rates on incomes for 1946 and 1947, and doubtless also for later years, will be lower than those on 1944 and 1945 incomes. This in turn will mean relatively larger taxable incomes. On this basis, a level of collections of something like 415 millions is indicated.

The next step is to take account of recent changes in rates and exemptions. The most important rate change relates to New York. In this state the rates for collections made during the fiscal year ended March 31, 1947, based on 1945 incomes, were only two thirds of the rates for the previous year. Collections were roughly 115 millions,[30] as compared with 148 millions for 1946; the decline of 33 millions was relatively smaller than the one-third decrease in effective rates.

A large part of this decline in New York, however, will be

---

with respect to 1946 taxes payable in 1947, but the full rates were to be applied thereafter. Letter from State Tax Commission, Apr. 19, 1947. At a special session in December 1947, taxes on 1947 and 1948 incomes were fixed at three fourths of the full rates, and deductions for married persons and dependents were increased by one half. Letter from State Tax Commission, Jan. 12, 1948.

[30] Letter from New York Department of Taxation and Finance, May 2, 1947.

offset by a rate increase approved in 1947. The soldiers' bonus act provides for an increase from 50 per cent to 60 per cent of the normal rates of 2 to 7 per cent, the revenues derived from the additional 10 percentage points to be allocated for financing the soldiers' bonus loan.[31] On the basis of recent yields, the revenues obtained from the additional 10 percentage points would amount to roughly 23 millions. Offsetting this estimated increase against the decrease of 33 millions, only 10 millions should be deducted from our previous estimate on account of the rate changes in New York.[32]

The increase in the Iowa rates to a three-fourths basis and the change in the Maryland rate from 2 to 2.5 per cent[33] will probably mean an increase of something like 5 millions in total state income tax collections. Other changes of minor revenue importance approved in 1947 include adjustments in rate schedules in Colorado, Vermont, and Oklahoma, and increased exemptions in Arkansas and Oklahoma.[34] Since some of these changes involve decreases in revenues, no further adjustment will be made in order to bring the estimate up to date.

Adding 5 millions for Iowa and Maryland to the previous figure of 415 millions, and deducting 10 millions for New York, the level of revenues at present rates and exemptions becomes 410 millions.

In marked contrast with developments in state sales taxes, there were no additions to the states imposing net income taxes in 1947. There are indications that the number of states using personal income taxes has become fairly well stabilized. On the other hand, some rate changes will almost certainly be made. The major uncertainty relates to New York. There

[31] Letter from Department of Taxation and Finance, Mar. 28, 1947. This increase will apply to incomes for 1947 and later years.

[32] This assumes that the tax will continue to be collected at 60 per cent of normal rates.

[33] *Tax Administrators News,* Vol. 11 (1947), p. 43.

[34] The same, pp. 16, 43, 55, 67.

is a strong likelihood that 1952 collections in this state will be at rates higher than 60 per cent of the basic rates—as at present. In order to take account of possible changes in rates in New York and other states, we have increased the estimate of 410 millions previously reached by 40 millions. Our final figure for 1952 thus becomes 450 millions.

III. DEATH AND GIFT TAXES

Every state except Nevada imposes some type of death tax. On the other hand, taxes on gifts are levied by only about one fourth of the states.[35] All but a small part of the revenues in this classification are obtained from inheritance and estate taxes.

In recent years revenues from death and gift taxes have fallen in the range of 100 millions to 175 millions. There was little change in revenues during the early war years. However, a rather sharp upturn occurred in 1945. The total for 1945 was 136 millions, and the yield for 1946 was 146 millions. The preliminary figure for 1947 is 166 millions. In the table on page 84, we have included 185 millions for these taxes in 1952.

Collections in the near future will be influenced by a number of factors. First, a level of values well above prewar now seems certain. Though adjustment to the new level will doubtless be slow, especially in states with appraisements by local officials, revenues for 1952 will be influenced to some extent by this factor. Second, during the war years there were marked increases in government bond holdings, savings funds, and bank deposits. These increases will affect postwar inventories of decedents. A significant factor in this connection is that exemptions for state death taxes are generally low, especially when compared with the federal exemption. Third, improved administration may also operate to increase revenues, but this is primarily a long-run factor.

[35] Tax Research Department, Commerce Clearing House, Inc., *Tax Systems*, 10th ed. (1946), pp. 250 ff.

IV. LIQUOR AND TOBACCO TAXES

Selective or special sales taxes imposed by the states have been limited mainly to those on liquors and tobacco products. Though the sumptuary basis for taxation is no longer emphasized, traditionally it accounts for singling out commodities such as liquor and tobacco for special tax treatment. As in the case of comparable federal taxes, the revenues derived are now a far more important consideration than any restrictive effects on consumption.

Liquor taxes. Each of the 48 states obtains some revenues from the liquor business. In those states in which the retail phase of the business is in private hands, excises and license taxes contribute importantly to state revenues. In addition to various tax sources, the 16 liquor-monopoly states derive substantial profits from operations; a major portion of these profits is ordinarily made available for general purposes.

In common with the federal liquor taxes, state revenues from taxes on alcoholic beverages rose rapidly during the war years. Revenues amounted to 255 millions for 1940. By 1943 the total had mounted to 335 millions and by 1945 to 368 millions. The comparable yield for 1946 was 469 millions; of this amount, 402 millions was derived from sales or excise taxes and 67 millions from license taxes. The preliminary total for 1947 is 482 millions.

The increase in state liquor taxes has been relatively much smaller than that for federal liquor taxes. The growth of state revenues was primarily a result of the enormous rise in consumption during the war period; prior to 1947 state rate changes were comparatively few and had little effect on revenues. In contrast, the increased rate for distilled spirits was a major reason for the sharp expansion of federal revenues.

Under the program in the table on page 84, state revenues from liquor taxes for 1952 would amount to 400 millions, a figure below recent yields. Considering that seven states[36] increased their rates in 1947 and that additional changes are

[36] Arkansas, Idaho, Iowa, Kansas, New Jersey, Tennessee, and West Virginia.

likely in the next few years, this figure may seem rather low. The sharp decline in consumption during the early months of the calendar year 1947 is the principal reason for what may appear to be an unduly conservative figure. Moreover, there is at least a possibility of some reductions in rates, on the theory that combined state and federal taxes have become too repressive.

Tobacco taxes. Both the number of states using tobacco taxes and the revenues derived are expanding rapidly. In 1946 only 31 states imposed excises on one or more tobacco products,[37] but 1947 enactments brought the total to 38.

From 1940 to 1946 state revenues from tobacco taxes more than doubled; the 1940 yield was 97 millions and that for 1946 was 199 millions. The increase for 1946 over 1945 was very large—from 145 to 199 millions—or roughly one third. Two factors contributed importantly to this sharp increase. First, collections for the fiscal year 1945 were affected by short supplies, especially during the early summer of 1945; revenues for 1945 were about 10 per cent below those for 1944. Second, the rapid demobilization of the armed forces during the fiscal year 1946 meant some increase in the sales taxable by the states. The preliminary figure for 1947 is 245 millions.

State revenues from tobacco taxes in the years immediately ahead will be strongly influenced by the seven new taxes adopted in 1947, together with rate increases in eight states.[38] The new taxes will probably mean an increase of about 40 millions in revenues, while the 1947 rate increases should produce additional revenues of perhaps 45 millions.[39] On this

[37] Commerce Clearing House, Inc., *Tax Systems*, 10th ed., pp. 195 ff.

[38] The new taxes are in Indiana, Michigan, Minnesota, Montana, Nebraska, Nevada, and West Virginia. Rate increases have been approved in Arkansas, Idaho, Kansas, Maine, New Mexico, New York, Pennsylvania, and Rhode Island. *Tax Administrators News*, Vol. 11 (1947), pp. 31, 40, 52, 68, and 78. The Oregon cigarette tax is not here included; this tax was rejected by the electorate in a referendum vote held Oct. 7, 1947.

[39] In arriving at this estimate, the increase in rate in Illinois from 2 to 3 cents, approved in 1946 and effective Jan. 1, 1947, has also been taken into account.

basis, the current yield is at an annual rate of about 320 millions.[40]

Recent developments suggest that additional adoptions and rate increases are likely during the next few years. Perhaps the best assumption is that new adoptions and rate increases will raise revenues by about as much as the 1947 adoptions and changes. Accordingly, in the table on page 84, we have included 400 millions for 1952 revenues from this source.

V. OTHER STATE TAXES

In this section we consider taxes on property, severance taxes, and a group of miscellaneous state taxes not elsewhere classified. These taxes are discussed before the important highway-user taxes for the reason that the revenues are used for general purposes.

Property taxes. From a position of pre-eminence, property taxes have gradually dwindled to their present status as a minor source of state revenues. Prior to World War I taxes on property accounted for well over one half of state tax revenues; in 1946 the proportion was only 5 per cent. The enormous expansion in local tax requirements was a major reason for this sharp decline. Since the property tax was generally the only important revenue source available to local governments, strong pressures were brought in many states for exclusive allocation to local governments. The development of special-purpose levies, especially the motor-vehicle taxes, was also a major factor bringing about the sharp relative decline in property taxes.

The decline in the relative importance of state property tax revenues will doubtless continue in the years ahead. Faced with a higher level of costs and the sluggishness of the property tax base, the case for exclusive local use of the property tax will be stronger than ever before. This observation applies particularly to the general or full-rate property tax.

[40] This figure is based on estimated fiscal year 1947 collections of 235 millions; the latter figure excludes collections resulting from the Illinois and other rate increases effective early in 1947.

Continued use by the states of special taxes such as low-rate taxes on intangibles, and also of various selective taxes usually classed as property taxes, is a virtual certainty. In the table on page 84, property tax revenues have been placed at 210 millions for 1952. Revenues for 1940 were 260 millions.

Severance taxes. Taxes classed under this heading include a variety of levies on the extraction of natural resources. Approximately one half the states use one or more taxes in this category. Included are: (1) the Minnesota occupational and royalty taxes on iron ore; (2) the Louisiana taxes on sulphur, gas, oil, turpentine, coal, oysters, and shrimp; and (3) the taxes imposed by Texas on sulphur, oil, gas, and ores.

Revenues from severance taxes amounted to only 53 millions for 1940. As activity in most lines expanded sharply during the war years, a sharp increase in revenues was to be expected. By 1943 revenues amounted to 75 millions. Following a slight decline in 1944, yields of 83 millions and 90 millions were reported for 1945 and 1946. The preliminary figure for 1947 is 94 millions. We have included 90 millions for severance tax revenues in 1952 in the table on p. 84.

Miscellaneous taxes. Taxes here classed as miscellaneous include: (1) those on insurance companies measured by premiums; (2) gross receipts and other special taxes on public utilities; (3) general corporation taxes, especially those based on capital stock; (4) hunting and fishing licenses; and (5) various minor taxes such as those on pari-mutuel betting and amusements.

Revenues from these miscellaneous taxes amounted to 449 millions in 1940; insurance taxes accounted for 102 millions and taxes on public utilities for 93 millions. The comparable figure for 1946 is 744 millions, of which insurance taxes represented 144 millions and the utilities taxes 152 millions. The preliminary total for 1947 is 827 millions. Under the revenue program shown on page 84, revenues from this group of taxes would amount to 825 millions for 1952. This figure assumes that there will be relatively few additions to the number and types of miscellaneous taxes.

VI. HIGHWAY-USER TAXES

The highway-user taxes have long been among the most productive state tax sources. They are here considered last for the reason that they are in the nature of special-purpose levies. Though these levies are collected under the taxing power, they are more nearly akin to service charges than to taxes imposed to finance other governmental functions. The proceeds—with some exceptions—are specifically allocated for highway construction and maintenance, together with the servicing of highway debt.

Motor vehicle fuel taxes. In contrast with most other state taxes, revenues from motor vehicle fuel taxes declined during the war. From a total of 839 millions in 1940, receipts dropped to 776 millions for 1943 and 685 millions for 1944. For 1945 receipts were 696 millions, almost the same as for 1944. Rationing of gasoline and tires and a reduction in the number of motor vehicles in operation were the major reasons for the wartime decline. On the other hand, revenues mounted rapidly after the end of the war. Net collections for the fiscal year 1946 were 887 millions.

A sharp expansion in revenues is now taking place. The preliminary figure for 1947 is 1,124 millions, an increase of about 27 per cent over 1946. Increased use made possible by rising supplies of tires and accessories, together with the increasing number of cars, contributed importantly to the rise. Another important factor is just beginning to influence revenues and will be of great significance in 1948 and 1949. At their 1947 legislative sessions eight states raised their gasoline taxes by amounts ranging from one half to 2 cents per gallon.[41] The three factors—increased use, larger number of cars, and higher tax rates—will mean further increases in revenues in 1948 and later years. In the table on page 84, we have included 1,325 millions for 1952 revenues from state motor vehicle fuel taxes.

[41] The eight states are California, Colorado, Connecticut, Maine, Maryland, Nevada, Rhode Island, and Vermont.

Motor vehicle license taxes. In contrast with the gasoline tax, revenues from motor vehicle licenses increased slightly during the war years. The 1940 yield was 387 millions. There were small increases in each of the next four years, bringing the 1944 total to 413 millions; the corresponding figure for 1945 is 414 millions.[42] Revenues increased sharply after the end of the war. Collections for 1946 were 461 millions, or about 10 per cent above 1945. The preliminary figure for 1947 is 540 millions.

The major factor in the present upward trend is the expanding number of motor vehicles. High production plus the current tendency to extract the last bit of use from old cars is causing a rapid expansion in the number of motor vehicles in operation. On the other hand, rate increases will doubtless be much less important than in the case of the gasoline tax.

In the table on page 84, we have included 600 millions for revenues from motor vehicle license taxes, including operators' licenses.

VII. NONTAX REVENUES

Revenues of state governments from sources other than taxes include charges for services and a variety of miscellaneous revenues such as interest, rents, fines and forfeits, escheats, and donations. Contributions to general revenues from the 16 state liquor monopolies and other state enterprises are not included.

Charges made for services rendered account for the bulk of state nontax revenues. For 1940 this classification showed a yield of 195 millions; receipts for 1946 are estimated at 240 millions. We have included 250 millions from this source for 1952. Because of the greater diversification of state tax systems, among other reasons, there is less pressure for increasing

[42] The small increases in revenues from motor vehicle licenses during the war years are difficult to explain, since there was a decrease in the number of passenger cars in operation. Re-registration in one or more additional states by workers changing jobs and others changing their domiciles was one factor holding up receipts from this source. Sale of cars by those entering the armed services to noncar owners was another factor, at least to the extent proportionate refunds were not obtained or were unobtainable.

state service fees than there is in the case of municipal governments.[43]

Miscellaneous state nontax revenues have amounted to less than 50 millions a year; for 1944 the yield was about 44 millions. We have included 50 millions for 1952 in the table on page 84.

[43] Payments to state educational institutions on account of veterans' education, as provided by the Servicemen's Readjustment Act, are not here included as service charges. The moneys involved have been counted at the federal level.

CHAPTER VI

LOCAL TAXES AND OTHER REVENUES

Local governments will need revenues of about 8.4 billions in 1952 in order to cover their expenditures, as estimated in Chapter II.[1] This figure includes local shares in state-collected taxes, but it does not include receipts from grants. Moneys transferred as grants, as previously explained, have been uniformly regarded as revenues of the first disbursing authority.[2] A distribution of local revenues for 1952 by sources, together with collections for 1940, is shown in the table on page 103.[3]

The local revenue estimates for 1952 assume that there will not be any major additions to the revenue sources now used by local governments. This assumption does not run counter to the view that greater diversification of revenue sources is needed if local governments are to be adequately financed. According to present indications, however, the disparity between functional requirements and available local revenue sources which has long characterized local (especially municipal) finance is likely to continue.[4]

[1] It is recognized that the 1952 revenue goal of local governments might be somewhat smaller than is here indicated. A portion of capital outlays will be financed from borrowings, and in some cases postwar reserves will also be drawn upon. Despite these facts, we believe it would be inadvisable to make any adjustments. In the long run, debt increases will be largely offset by allocations to sinking funds and other requirements for debt service. Moreover, the reserve funds are of little more than temporary significance.

[2] The practice here followed corresponds to that used by the U. S. Bureau of the Census for 1940 and earlier years. For more recent years the Bureau has classed local shares in state taxes under grants. In order to maintain comparability with 1940, we have followed the former procedure.

[3] The indicated increase in local revenues from 1940 to 1952 is almost 2.9 billions, or roughly 52 per cent. The comparable increase for local functional costs is almost 60 per cent. The difference between the two percentage figures results from the fact that the estimated increase in grants received by local governments is relatively larger than that for locally collected revenues.

[4] See *Federal, State, and Local Government Fiscal Relations*, S. Doc. 69, 78 Cong. 1 sess., pp. 8 ff.

Local Taxes and Other Revenues, Estimates for the Fiscal Year 1952 Compared With 1940

(In millions of dollars)

Source	1940	1952
Taxes:		
Property taxes	4,300	6,020
General and retail sales taxes	66	250
Income taxes	20	50
Special sales and excises	24	75
Taxes on specific businesses	179	400
Motor vehicle licenses	24	35
Other nonbusiness licenses	50	75
Miscellaneous	15	40
Total locally collected taxes	4,678	6,945
Shares in state-collected taxes	271	450
Total taxes	4,949	7,395
Nontax revenues:		
Special assessments	102	150
Charges for services	330	660
Interest and rents	107	150
Other nontax revenues	51	80
Total nontax revenues	590	1,040
Total tax and nontax revenues	5,539	8,435

I. PROPERTY TAXES

Local governments in the United States have always depended on property taxes for the greater part of their revenues. In recent decades, however, there has been some decline in the relative importance of this source. Thus, in 1922 property taxes accounted for 94 per cent of all local tax revenues, while in 1930 about 92 per cent of local taxes were derived from this source. The comparable proportion for 1940 was roughly 87 per cent and for 1946 it was about the same.[5]

Under the revenue program on this page, property taxes of local governments would amount to over 6 billions in 1952. The indicated increase from 1940 to 1952 is 1.7 billions, or 40 per cent. For a tax that is notoriously inelastic and has been generally regarded as unadaptable to large and sudden

[5] For all municipal governments, as distinct from combined local governments, the proportion is somewhat smaller.

increases in revenue needs, this is a very substantial rise. In particular, so large an increase runs counter to the view, which was widely held in the prewar years, that the productivity of the property tax has about reached its practicable limits.

Recent and current trends suggest that under present conditions property taxes are capable of considerable expansion. Because of their importance for local finance, we shall discuss these trends in detail.

There was some increase in local property taxes during the war years. Between 1940 and 1943 combined state and local property taxes rose by roughly 200 millions.[6] A further increase occurred between 1943 and 1945, bringing the combined state and local total for the later year to over 4.9 billions. Of the latter amount, local governments accounted for 4,640 millions.[7] To some extent, increased collections—especially during the early war years—resulted from the collection of delinquent taxes; tax delinquency was generally reduced to very low figures.

Local property taxes have risen sharply since the end of the war. The increase in local collections in 1946 was about 265 millions and the trend has since been sharply upward. Local tax rates are rising in most areas. Contrary to a widely held view, property-tax rates have not generally reached their maximum attainable limits. The impression that they have is mainly an outgrowth of the experience of some of the larger municipal governments and the resistance to further increases, which has at times developed.

For example, in Massachusetts 292 cities and towns reported increased rates for 1946 taxes payable in 1947, ranging from

[6] The national income unit of the Department of Commerce estimated combined state and local property taxes at 4.6 billions for 1943, as compared with 4.4 billions for 1940. *Survey of Current Business*, April 1944, p. 10. These are calendar year estimates.

[7] Virtually the entire increase in property taxes during the war years accrued to local governments. Property taxes collected for the account of state governments amounted to 260 millions for 1940 and 276 millions for 1945. The 1945 total was abnormally large because of the collection of 45 million dollars in back railroad property taxes and interest in New Jersey. The preliminary total for 1947 is 262 millions.

10 cents to $20 per $1,000 of assessed valuation; in 37 cities and towns the rate was the same as for the preceding year; and only 22 cities and towns reported reduced rates, with most of the decreases in the range of 10 cents to $5 per $1,000.[8] These data are of particular interest for the reason that Massachusetts is classed as an urban state. It is also a state in which considerable attention has long been given to property tax burdens and possible means of lessening them.

For the nation as a whole, increases in city tax rates up to 1946 were fairly moderate. Thus, the average tax rate of 249 American cities increased by only $1.75 per $1,000 between 1941 and 1946, or from $39.48 to $41.23. Adjusted to take into account the prevailing ratios of assessed to true value, the increase was only 75 cents per $1,000, or from $27.34 to $28.09. It is significant, however, that 52 cents of the 75-cent increase was accounted for by the increase for 1946 over 1945. A comparable tabulation for 1947 indicated a decrease in the adjusted tax rate of 5 cents per $1,000, or from $28.09 to $28.04.[9]

The rates imposed for school purposes appear to be increasing most rapidly. For example, in Iowa, Kansas, and Nebraska, increased levies for public schools have accounted for the bulk of the sharp rise in total property levies since 1944. Higher tax rates account for most of the increases in these states; taxable valuations have shown relatively small changes. In some states the pressure for school funds has necessitated amendments to levy limitations; South Dakota is an example.[10]

[8] *New York Times,* Dec. 1, 1946, sec. 1, p. 51. The rates here referred to are for all levies on property—not merely those for city or town purposes. Under the Massachusetts system, taxes are imposed by the state and counties on the cities and towns. Since the property tax is the principal flexible element, these taxes are in effect reflected in local property tax rates.

[9] "Tax Rates of American Cities," *National Municipal Review,* Vol. 35, December 1946, p. 570 and Vol. 37, January 1948, p. 16.

[10] The South Dakota legislature meeting in 1947 increased the limit for independent school districts from 25 mills to 40 mills. A county-wide levy for the payment of tuition of pupils of common school districts attending high school outside their own school districts was also authorized; districts operating an accredited four-year high school are excepted. Letter from Division of Taxation, May 2, 1947.

Upward adjustments in taxable valuations are now being made. At least three factors are contributing to the rise in taxable values. First, property values have risen both sharply and unevenly. It is now generally agreed that property values will be well above those of prewar years.[11] Second, in some areas government-owned properties acquired or developed to meet wartime needs are being returned to private ownership and added to the tax rolls. Third, new buildings are coming on the tax rolls. Despite the impediments to construction activities during 1946 and 1947, there was considerable private construction; a further upward swing in the immediate future seems likely.[12]

Mainly because of these factors, assessed valuations in most areas are now showing an upward trend. Thus, for the 249 cities previously referred to the average per-capita assessment for 1946 was 5.3 per cent larger than that for 1945. The comparable increase reported for 1947 is 15.7 per cent. The latter increase was substantially larger than that for any other recent year. For the period 1941 to 1946 the increase was 10.5 per cent.[13]

Rising tax rates combined with the upward trend in assessed valuations have meant sharp increases in property tax levies. Thus, for the 12 states included in the table on page 107 the increase in taxes payable in 1947 over those payable in 1940 averaged about 32 per cent. For a number of other states,

[11] In some areas adjustments in valuations for the property tax are just beginning and in others they have not yet begun. The gradual nature of the adjustments to a changed level of values is not solely a result of the inertia of assessment officials. In a number of states real estate, which comprises the bulk of the tax base, is assessed biennially or quadrennially; in several states the interval is in excess of four years.

[12] One offsetting factor may be noted. Veterans' exemptions will tend to retard the growth of the property tax base. For example, on Nov. 5, 1946 Louisiana adopted a constitutional amendment increasing the homestead exemption of World War II veterans from $2,000 to $5,000 for the period 1947–52. In Iowa it has been estimated that veterans' exemptions will amount to upwards of 100 millions, or something like 3 per cent of the tax base.

[13] "Tax Rates of American Cities," *National Municipal Review,* December 1946, p. 572 and January 1948, p. 16.

for which complete data for 1947 were not available, marked upward trends were reported. In all cases the larger part of the rise since 1940 has been concentrated in the years since the end of the war.

LOCAL PROPERTY TAXES PAYABLE IN 1947 COMPARED WITH THOSE PAYABLE IN 1940, TWELVE SELECTED STATES [a]

State	Taxes Payable (In millions of dollars)		Increase 1940 to 1947 (Per cent)
	1940	1947	
California [b]	293.7	468.5	59.5
Colorado	37.1	48.0	29.4
Indiana [c]	104.4	141.9	35.9
Iowa [d]	91.5	124.0	35.6
Kansas	59.4	76.4	28.6
Minnesota	102.4	128.0	25.0
Nebraska	40.3	53.9	33.9
Tennessee [e]	23.6	31.1	31.4
Utah	17.2	23.2	34.9
West Virginia	28.7	31.0	8.0
Wisconsin	108.8	145.1	33.4
Wyoming	7.7	10.0	29.1

[a] Data obtained from reports of and correspondence with state taxing authorities.
[b] Includes general property and solvent credits taxes.
[c] Figures include amounts for state purposes.
[d] Total local levies before deduction of taxes canceled by homestead credits.
[e] County levies only.

The present upward trend in tax levies appears to be general in character. The increases have not been restricted to any class of government. The levies for school purposes, however, have generally shown the largest relative increases. On the other hand, there are indications that the increases in the larger cities have frequently been smaller than comparable increases for all local governments combined. Nevertheless, some cities have reported very marked rises. For example, Detroit's total levies—city and school—amounted to 97 millions for 1946–47, an increase of 43 per cent over the com-

parable total of 67.6 millions for 1939–40.[14] For Minneapolis 1946 levies are reported at 28.9 millions, as compared with 21.4 millions for 1939, an increase of almost 35 per cent.[15]

The foregoing analysis suggests that a substantial part—perhaps one half or more—of the indicated increase in local property tax collections had been attained by 1947. If this is correct, an average annual increase for the next five years of less than 200 millions would be necessary for our estimate of 6 billions to be realized. Considering the marked rise in public school costs for 1947–48, among other factors, this figure may well prove to be conservative.

In concluding the discussion of local property taxes, mention should be made of the relation between administration and revenues. Improvements in administration will unquestionably contribute to the rise in property tax revenues. With growing demands for revenues, increasing attention is being given to the quality of administration, especially assessment methods and procedures. As has been well stated, the "possibilities for more effective property tax assessment administration are almost innumerable."[16] However, it would be easy to overemphasize the possibility of substantial betterments over a period of five years. But for the longer run this factor may be of major importance.

II. OTHER LOCALLY COLLECTED TAXES

Locally collected taxes other than the property tax include: (1) general and retail sales taxes; (2) income taxes; (3) special sales taxes and other excises; (4) taxes on specific businesses; (5) motor vehicle licenses; (6) other nonbusiness

[14] Detroit Bureau of Governmental Research, *Background for Budgeting*, March 1947, p. 7.

[15] Letter from Board of Estimate and Taxation, Apr. 11, 1947. Levies for state purposes are not included.

[16] E. L. Maynard, "Practical Possibilities for More Effective Property Assessment Administration," National Tax Association, *Proceedings* (1944), p. 319. Mr. Maynard observes that while some states have instituted programs of betterment, much remains to be accomplished. There are "other states that, regrettably, have yet to recognize the inadequacy of their property tax administration and to adopt the measures and policies that have gained acceptance and support wherever any premium is placed upon efficiency and equity in public management." The same, p. 312.

licenses; and (7) miscellaneous taxes. In 1940 the combined revenues obtained from these taxes amounted to about 380 millions, or roughly 8 per cent of all locally collected taxes. For 1952 we have included 925 millions.

Expansion of local revenues from these sources will be influenced by enabling laws approved during the 1947 sessions of state legislatures. For example, New York county and city governments have been granted the power to levy special taxes which would yield an estimated 111 millions, if used by all eligible units.[17] Even broader revenue-raising powers were granted local governments in Pennsylvania.[18]

General and retail sales taxes. In 1940 the yield of locally administered general and retail sales taxes was 66 millions. The largest part of the revenues in that year was accounted for by the New York City sales and use taxes, which amounted to 55 millions. New Orleans ranked second with revenues of about 1.5 millions.[19] Other cities imposing sales taxes in 1940 included Charleston and Huntington, West Virginia. In contrast with the New York and New Orleans taxes, these levies are of the general type. The rates in both cities have been very moderate.[20]

The present upward trend in local sales tax revenues is strongly influenced by recent adoptions. In 1945 and 1946 Los Angeles and a number of smaller California cities enacted ordinances imposing sales taxes.[21] In early 1947 no less than

[17] *New York Times,* Mar. 25, 1947, p. 1.

[18] Act 481 of 1947.

[19] The New Orleans tax in effect during 1940 was a 1 per cent general retail sales tax. The city tax was collected by the state along with the state tax, and the proceeds—less costs of collection—were remitted to the city. The net yield to the city was about 1.4 millions. At present New Orleans collects its own tax at the rate of 2 per cent. Letter from New Orleans Bureau of Governmental Research, May 5, 1947.

[20] A. M. Hillhouse and Muriel Magelssen, *Where Cities Get Their Money* (1945), p. 52. Taxes often classed as sales taxes were also imposed by St. Louis and Kansas City. These taxes, however, are probably best classed as license taxes.

[21] The smaller cities here referred to include Oakland, San Diego, Berkeley, Santa Ana, San Bernardino, Santa Barbara, and ten smaller places. Edward Roesken, "Municipal Income, Sales and Use Taxes," *Taxes,* Vol. 24, October 1946, p. 976.

53 California cities were collecting sales taxes. The rate in 11 cities is 1 per cent and in 42 cities one half per cent. Annual revenues of 45 cities for which estimates are available are placed at 14.2 millions. Of this total, Los Angeles accounts for 7.2 millions.[22]

Erie County, New York, imposed a 1 per cent sales tax effective July 1, 1947, the proceeds to be employed for school purposes. The City of Syracuse recently passed a sales tax effective March 1, 1948; the rate is 2 per cent. The proceeds of this tax may be used for general city purposes. Though the special enabling law referred to requires that counties employ the taxes for school purposes, cities are not so restricted.

In the table on page 103, we have included 250 millions for local sales tax revenues in 1952. This figure assumes that the New York City tax will be continued at the rate of 2 per cent. Sales tax revenues of this city are currently estimated at about 120 millions a year.

Income taxes. Under the revenue program on page 103, local income-tax revenues would amount to 50 millions for 1952. In 1940 the yield was only 20 millions; virtually the entire amount was collected by Philadelphia and Washington, D. C.

Prior to 1940 taxes on net income for local purposes were collected only in the District of Columbia. In the immediate prewar years, the combined revenues from the District's individual and corporate taxes ranged between 1 and 2 millions. All the revenues accrue to the District government, which is coterminous with the city of Washington.[23]

Philadelphia has levied a tax on salaries and wages since 1940. This tax applies to the entire salaries and other compensation of individual residents of the city and to salaries and

[22] Richard Graves, "Sales Tax in 53 California Cities," *Western City*, March 1947, p. 24.

[23] The District of Columbia income taxes are often classified as state income taxes. We have here classed them as local taxes for the reason that the revenues accrue to a government whose functions correspond in the main with those of other large municipalities. The laws imposing these taxes were enacted by the Congress of the United States.

other compensation of nonresidents for work done or services performed within the city. Employers are required to withhold the tax and to make monthly returns. The tax also applies to the net business profits of trades, businesses, professions, and other enterprises operated by residents, and to profits of similar nonresident enterprises to the extent conducted in the city of Philadelphia. However, this tax is not applicable to corporations which pay a state income tax.[24] The present rate of tax is 1 per cent; for the first few years it was 1.5 per cent. In recent years revenues have ranged from 20 millions to about 25 millions.

Two additional cities—Toledo and St. Louis—adopted local income taxes in 1946. The Toledo tax applies to salaries, wages, and other compensation earned after March 1, 1946. Included in the tax base are the net profits of businesses, professions, and other activities. Income of nonresidents is taxed to the extent earned in the city. Withholding and quarterly payments are required. In contrast with the Philadelphia tax, the allocated net profits of corporations are subject to the Toledo tax. The rate of tax on all classes of taxable income is 1 per cent. Revenues have been estimated at 4 millions for 1947 and 5 millions annually for 1948–50.[25]

The scope of the St. Louis income or earnings tax, which became effective on August 1, 1946, was comparable with that of the Toledo tax. This tax, however, remained in effect less than a year. It was declared unconstitutional by the circuit court of St. Louis in the spring of 1947.[26] The decision of the lower court was later upheld by the Missouri Supreme Court.[27]

[24] Pennsylvania imposes a tax on the incomes of corporations, but not on individual incomes or incomes earned by other forms of business organizations. A statutory provision prohibits first- and second-class cities from taxing subjects already taxed by the state. Philadelphia is the only first-class city. Roesken, "Municipal Income, Sales and Use Taxes," *Taxes*, p. 972.

[25] *The Toledo City Journal*, Oct. 19, 1946, p. 583.

[26] *National Municipal Review*, Vol. 36, April 1947, p. 229.

[27] *Tax Administrators News*, Vol. 11, p. 67.

Columbus, Ohio, recently adopted an income tax effective January 1, 1948. The rate is one-half per cent and the tax is to remain in effect for five years. This tax applies to wages, salaries, and other compensation for personal service, and to the net profits of professions, unincorporated businesses, and corporations. The yield for 1948 has been estimated at 2.5 millions.[28]

Other communities have considered local income taxes of the type here discussed, but thus far adoptions have not been frequent. Though the Philadelphia type of levy is rated a good metropolitan tax,[29] the rapid extension of locally administered income taxes does not appear imminent.

Special sales taxes and other excises. Included in this classification are local taxes on the sale of tobacco and gasoline, together with the New York City taxes on business gross income.[30] Revenues for 1940 were reported at about 24 millions. We have included 75 millions for 1952 in the table on page 103.

Since 1940 the number of local governments levying special local sales taxes on cigarettes and tobacco products has expanded greatly. The 1946 additions include Miami, Omaha, St. Joseph, and Wheeling.[31] At the end of 1946 there were 35 cities that imposed cigarette taxes at one or two cents a pack. No less than 32 of these cities were in Alabama, Florida, and Missouri.[32] Baltimore is a recent addition to the cities taxing tobacco products.[33]

[28] The same, Vol. 11, p. 137.

[29] A major problem confronting many large cities is how to reach the outsider who benefits from the city's services. Philadelphia's "daylight citizens" have been contributing between 6 and 7 millions annually, or roughly one third of the local income tax yield. Hillhouse and Magelssen, *Where Cities Get their Money*, p. 107.

[30] Strictly speaking, the local taxes on alcoholic beverages not imposed as license taxes belong in this group. However, these taxes were included under "taxes on specific businesses" in the basic data used for 1940, and we have retained the same classifications for 1952. In 1940 local taxes on consumption of alcoholic beverages were a very minor item.

[31] Tax Institute, *Tax Policy*, November 1946, p. 9.

[32] "Trends in Municipal Tax Revenues and Service Charges," *Public Management*, Vol. 29, April 1947, p. 102.

[33] Hillhouse, *1947 Supplement to Where Cities Get Their Money*, p. 8.

Taxes on the sale of gasoline were levied by 242 cities at the end of 1946; included are a number of cities of less than 5,000. All but 12 of these cities are in Alabama, Missouri, and New Mexico. The rates range from a fraction of a cent to three cents per gallon.[34]

Taxes on specific businesses. This classification includes special taxes on corporations and public utilities, companies selling alcoholic beverages, local taxes on amusements, and a variety of minor business taxes. Most of these levies are imposed as license taxes. Revenues for 1940 amounted to 179 millions. In the table on page 103, we have included 400 millions for these taxes in 1952.

A number of cities have revamped their business license schedules with a view to increasing their productivity. Those reported in the period 1942–45 include Detroit, Boston, Madison, Wisconsin, Fort Myers, Florida, and four California cities—Sacramento, San Bernardino, Alameda, and Richmond.[35] More recently, increased rates have been made effective in New York City, Los Angeles, and Charlotte, N. C., among other cities.[36] Special utilities taxes are also being used by an increasing number of cities. Additions in 1946 included Portland, Oregon, and Youngstown, Ohio. Long experience with business license taxes, together with the fact that an administrative mechanism is already at hand, is a strong reason favoring increased use of this form of levy.

Business license taxes at moderate rates often produce substantial revenues. For example, in 1946 New York City raised 13.6 millions from a low-rate license tax on gross receipts. In the same year Seattle obtained 1.5 millions from a similar tax and Kansas City collected $643,000.[37]

In the opinion of some, higher rates for and additions to

[34] "Trends in Municipal Tax Revenues and Service Charges," *Public Management*, p. 102.

[35] Hillhouse and Magelssen, *Where Cities Get Their Money*, p. 20.

[36] Hillhouse, *1947 Supplement to Where Cities Get Their Money*, pp. 4–5.

[37] "Trends in Municipal Tax Revenues and Service Charges," *Public Management*, p. 101.

business license taxes represent the most logical solution of the revenue problems of the cities.[38] While it is not likely that revenues will rise to a point where they will constitute a major source of income, a fairly pronounced expansion seems probable, especially in the case of larger municipalities that are hard pressed for additional funds.

Motor vehicle licenses. Local motor vehicle license taxes accounted for revenues of less than 25 millions in 1940. We have included 35 millions for 1952 in the table on page 103.

An important reason for the comparatively small revenues from this source is that in most states the cities do not have authority to levy a motor vehicle license tax, registration fee, or wheelage tax. In 1945 this form of tax could be imposed for municipal purposes in only 12 states[39] and was being used by cities in only 10 of the states. The exceptions were Minnesota and South Dakota. Municipalities were specifically forbidden to impose registration taxes in 24 states and are "evidently" forbidden in three others. In 9 states there was neither a statutory denial of this right nor a specific authorization. In 4 states the counties were authorized to levy registration taxes, in 29 states this right was specifically forbidden, and in 14 states the law was silent.[40]

The most extensive use of local motor vehicle license taxes is found in Illinois, Missouri, North Carolina, Virginia, Arkansas, and Kentucky. Large cities deriving substantial revenues from this source include Chicago, St. Louis, Kansas City, Louisville, and Richmond.[41]

Other nonbusiness license taxes. In 1940 local governments obtained about 50 millions from nonbusiness license taxes including permits. Licenses and permits for building construc-

[38] See, for example, Malcolm M. Davisson, *Business License Taxes: A Major Potential Source of Municipal Revenue,* Report No. 37, League of California Cities, September 1945.

[39] The twelve states are Arkansas, Illinois, Kentucky, Minnesota, Missouri, Nebraska, Nevada, North Carolina, South Dakota, Tennessee, Utah, and Virginia. Hillhouse and Magelssen, *Where Cities Get Their Money,* p. 84.

[40] The same.

[41] The same.

tion and regulatory licenses of various kinds account for a substantial part of the total. Charges for street and highway use are also of some importance. In the table on page 103, revenues for 1952 are placed at 75 millions.

Miscellaneous local taxes. Taxes not elsewhere classified accounted for revenues of 15 millions in 1940. Included in this total are poll taxes, the New York City tax on racing, local death taxes, and a variety of other levies of minor revenue importance. In the distribution for 1952, we have included 40 millions for revenues from these sources.

III. LOCAL SHARES IN STATE TAXES

"Shared state tax" is used to describe those state-imposed taxes which are shared with local governments in proportion to—or substantially in proportion to—the revenues collected in or produced by the local units. "Local share" refers to the portion of the receipts collected for or accruing to local governments. A state grant-in-aid, on the other hand, is a payment of state funds to local governments for the support of specified functions or general governmental purposes, without regard to the local jurisdiction in which the revenues were collected.[42]

Though the distinction between local shares and state grants is regarded by some as less significant than formerly,[43] it has been retained in the present study. One reason for this decision was that this distinction had generally been made in statistical compilations for 1940. Recently, another reason for distinguishing between local shares and grants has become of considerable importance. If state tax moneys are to be apportioned in a manner that will benefit many of the hard-pressed

[42] When it is desired to refer to both local shares and grants, "aids to other governments" is now commonly used.

[43] Prior to 1941 a sharp distinction was drawn between local shares and grants in the statistical compilations of the United States Bureau of the Census. Local shares were excluded from state revenues and accounted for as agency receipts; in turn, the amounts involved were treated as tax revenues of the local governments receiving them. Moneys transferred as

city governments, allocation on the basis of collections rather than some formula designed to measure need will be essential. Since the cities are usually the best economic units, they are generally not interested in aid formulas which emphasize needs and the maintenance of minimum standards in the performance of specific governmental functions.

We do not wish to imply that a much greater expansion in local shares than in grants is to be expected. On the contrary, equalization grants are likely to receive more consideration than urban claims for shared taxes. Without minimizing the seriousness of the revenue problems of the cities, many of the poorer economic units are also faced with pressing revenue needs. A significant factor in this connection is that most state legislative bodies are more interested in the problems of the rural sections. In some instances they are even anti-urban in their reactions to the fiscal problems of the cities.[44] Mainly because of the geographic and economic composition of most state legislatures, the trend in local shares will at best be only moderately upwards; an expansion so sharp as to affect materially the distribution of local revenues by sources is not probable.

Supplemental optional local rates. It has been suggested that, as an alternative to shared taxes, local governments be given the authority to add supplemental rates to certain existing state taxes. Revenues derived from the supplemental rate, less a proportionate part of the costs of administration, would be returned to the city or other local unit. Several advan-

grants, on the other hand, were included in state tax or other revenues, and reported as grant-in-aid receipts by local governments. In later years the distinction between local shares and grants has not been emphasized in the publications of the Bureau. Local shares have been counted as revenues of the paying government and listed under "aids from other governments" in the gross revenues of the receiving government. At the time this change was made, there seemed to be good reasons for the departure from the previous practice. In particular, there were certain borderline cases which might presumably be classed either way, and expert opinion often differed concerning the best classification for particular items.

[44] Harold L. Henderson, "State Aids as a Possible Revenue Source for Cities," *Bulletin of the National Tax Association,* Vol. 32, November 1946, p. 43.

tages are claimed for this plan. First, the principle of home rule is upheld; the local government's legislative body decides whether a supplemental rate shall be imposed. Second, the optional feature of the plan meets the diverse needs of the cities or other local units; many cities may have no need for the additional revenues.[45]

At this juncture it is not possible to forecast whether the revenues derived from supplemental rates will play a significant role in local finance—especially municipal finance—in the years ahead. It seems certain, however, that this proposal will be considered by some state legislatures. Such a plan has been specifically recommended to the Michigan legislature by a special interim legislative committee. This committee suggested that the state reduce its rate for the retail sales tax from 3 per cent to 2½ per cent, and at the same time grant the cities the authority to levy a supplemental rate of one-half per cent.[46]

In the revenues for 1952 shown in the table on page 103, we have included 450 millions for local shares in state taxes, including revenues from supplemental rates. In 1940 local shares amounted to 271 millions.[47]

IV. NONTAX REVENUES

Local governments collect substantial revenues from nontax sources. These revenues may be conveniently classed under special assessments, charges for services, interest and rents, and miscellaneous nontaxes.[48] In 1940 the combined revenues from

[45] The same, p. 47.

[46] *Preliminary Report of the Michigan Tax Study Advisory Committee,* January 1945, pp. 21–24.

[47] The indicated increase over 1940 is proportionately smaller than that for state grants received by local governments. One reason for the difference is that the state of New York has recently abandoned its system of shared taxes in favor of per-capita grants. *Session Laws* (1946), Chap. 301.

[48] Grants received from other governments are not included. Our analysis relates only to revenues derived from local sources, which are here defined to include local shares but to exclude grants. Also excluded are contributions from public service and other business enterprises. It is estimated that in 1952 contributions from these enterprises to general revenues will exceed contributions to such enterprises by 60 millions.

these sources amounted to 590 millions. Under the revenue program for 1952 shown in the table on page 103, slightly over 1 billion dollars would be obtained from nontax receipts.

Special assessments. Special assessments are benefit levies made mainly for the purpose of financing capital outlays such as street construction and sewers.[40] In theory, the properties against which the levies are imposed derive a direct benefit equal to the assessment. In 1940 local governments obtained slightly over 100 millions from this source. For 1952 revenues from special assessments have been placed at 150 millions.

When one considers the large expenditures on urban street construction and improvements that are expected over the next three to five years, the increase here estimated may appear rather moderate. However, there is one important factor working in the opposite direction. Experience with special assessment financing has frequently been far from satisfactory. Moreover, this type of financing has often proved to be decidedly uneconomical. In many communities it has come to be regarded with disfavor by both public officials and contractors.

Charges for services. Local governments perform a variety of services for which specific charges or fees are imposed. Included among these are court costs and fees, recording fees, police charges, protective inspection fees, bridge and tunnel tolls, hospital charges, various school and library revenues, and fees covering admission to and use of recreational facilities, together with other items.

In 1940 local governments collected 330 millions from service charges of all kinds. We have included 660 millions for 1952 revenues from this source. This figure assumes a sharp expansion in revenues of urban governments, especially the larger cities, and moderate increases for county and other local governments. In recent years a number of cities have either increased the range of service charges or raised the rates

[40] A number of cities levy special assessments to meet certain current or operating expenses. These assessments are here classed under "charges for services."

for existing charges. Similar action is currently being considered by other municipalities.[50]

Interest and rents. Local revenues from the use of public money and property amounted to about 107 millions[51] for 1940. We have included 150 millions for 1952.

Because of the improved current or cash position of many local governments, interest income will no doubt show sharp increases in some cases. Interest earnings on federal bond holdings will help to swell the total. An offsetting factor is that interest rates are somewhat below prewar levels. In general, income from rents will doubtless show smaller rises than interest. To the extent that public properties are rented under long-term agreements negotiated in prewar and the early war years, the rise in total rental income will be retarded.

Other nontax revenues. This miscellaneous classification includes fines, forfeits, escheats, and donations from private sources. Revenues for 1940 were 51 millions. For 1952 we have included 80 millions.

[50] A number of cities have introduced charges for garbage collection in recent years. In 1946 Cincinnati, Dallas, Detroit, and St. Paul, among other cities, imposed charges for such service. *Tax Policy,* Vol. 13, November 1946, p. 8. See Also Hillhouse, *1947 Supplement to Where Cities Get Their Money,* pp. 17 ff.

[51] This figure includes a small amount for royalties and net proceeds from the sale of property.

CHAPTER VII

SOCIAL SECURITY FINANCES

The discussion in preceding chapters has not included expenditures payable through the social security trust funds or the pay-roll taxes. These expenditures and revenues must be taken into account if a complete fiscal picture is to be presented. Though nominally the social security taxes are unavailable for general governmental purposes, in practice revenues in excess of cash payments through the trust funds are used to finance general functions or to retire debt held by the public.

I. OLD-AGE AND SURVIVORS INSURANCE TRUST FUND

Expenditures. Benefits payable in 1952 through the old-age and survivors insurance trust fund are estimated at 840 millions to 950 millions—with no change in coverage.[1] The probable expenditure is placed at 900 millions.[2] Adding 40 millions for administrative expenses payable through the fund, the total becomes 940 millions.

Larger amounts would be required if the coverage of the old-age insurance system should be extended.[3] Though it is probable that some extensions will soon be approved, they are difficult to gauge in time. After considering all factors, extensions and increases in benefits calling for an increase of one fifth in expenditures might be approved within the next four

[1] Estimated on the basis of the trend indicated by recent estimates for 1947–51 prepared by the Social Security Administration, and published in *Seventh Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance Trust Fund,* S. Doc. 18, 80 Cong. 1 sess., p. 10.

[2] Benefits paid during the fiscal year 1947 were 426 millions, an increase of 105 millions over 1946. U. S. Treasury Department, *Daily Treasury Statement,* June 30, 1947, p. 3.

[3] A study made a few years ago indicated that in 1944 only 30.4 million out of 51.8 million employed civilians were covered by the old-age insurance system. Of those excluded, railroad workers and many federal, state, and local employees are covered by separate retirement plans. The self-employed, agricultural laborers, domestic service workers, and employees of nonprofit institutions were the major groups not covered under the old-age system. *Issues in Social Security,* A Report to the Committee on Ways and Means by the Committee's Social Security Technical Staff (1946), p. 26.

years. On this assumption, 1952 benefits would be about 1,080 millions. Including 50 millions for administration, the total becomes 1,130 millions.

Cash receipts. Revenues from the federal old-age taxes are currently running at the rate of almost 1.5 billions a year, or well over double those for 1940. Total cash receipts credited to the fund in 1947 amounted to 1,459 millions, as compared with 1,238 millions for 1946. In these years the rates were the same as at present; that is, 1 per cent on employers and 1 per cent on employees, or a combined rate of 2 per cent of taxable pay rolls.[4]

Revenues collected in 1952 will be influenced principally by three factors: (1) the rates in effect; (2) the level of business activity; and (3) whether or not coverage is extended. Under the law now in effect, the rate for each tax will remain at 1 per cent for the calendar years 1948 and 1949. For 1950 and 1951 the rate will be 1.5 per cent, and for 1952 and thereafter it will be 2 per cent.[5] The average rate for taxes collected during the fiscal year ending June 30, 1952 will therefore be about 1.6 per cent, or a combined rate of 3.25 per cent.[6]

The next step is to consider the probable pay-roll base under present coverage. For the period to which collections for the fiscal year 1946 relate, income payments were about 160 billions, and wages and salaries paid by others than government were roughly 79 billions.[7] Collections of 1,238 millions indicate taxable wages and salaries of 61.9 billions, or 78.3 per cent of the total for the private sector of the economy. We shall use the latter figure in our approximations for 1952.

In 1951–52 the base for the old-age tax under present cov-

[4] Taxable wages include noncash remuneration; they do not include any amounts in excess of $3,000 per year. *Internal Revenue Code,* sec. 1426 (a). These taxes apply to wages paid to or received by persons engaged in all types of employment not specifically excluded. The exclusions are enumerated in sec. 1426 (b).

[5] Public Law 379, 80 Cong. 1 sess.

[6] The old-age taxes are payable quarterly and there is a lag of about three months. Under present practice three of the four quarterly collection dates for calendar year 1951 taxes would fall within the fiscal year 1952.

[7] These figures are for the 12 months ended Mar. 31, 1946.

erage will probably be well above that for 1945–46. Total private wages and salaries, according to present indications, will be relatively larger and aggregate governmental wages and salaries smaller than in 1945–46. With income payments at 165 billions, private wages and salaries would perhaps be 90 billions. Applying the ratio of 78.3 per cent, the taxable portion of pay rolls may be estimated at 70 billions. At an average combined rate of 3.25 per cent, the yield would be roughly 2,275 millions.

Taxable pay rolls would be substantially larger if coverage is extended. To take account of this contingency, we shall assume that increases in coverage will result in roughly a one-fifth increase in the tax base. On this basis, the yield would be 2,730 millions.

II. RAILROAD RETIREMENT ACCOUNT

Expenditures. Railroad retirement benefits are estimated at 240 millions for 1952. Including 5 millions for administration, the probable expenditure becomes 245 millions. The range is placed at 230 millions to 260 millions.

The estimate of 240 millions for benefits payable in 1952 assumes only a moderate increase over the revised estimate of 228.5 millions for 1948.[8] The significant fact, however, is that—as a result of liberalizing amendments approved in 1946[9]—annual requirements are now well above those of earlier years. For the fiscal year 1946, total benefits were only 152 millions.

Cash receipts. Railroad retirement taxes have risen sharply in recent years. Collections for 1940 were 121 millions. By 1944 the total reached 267 millions, and for 1946 collections were 283 millions. The original budget estimate for 1948 was 487 millions; the revised figure is 557 millions.

The upward trend in revenues has resulted mainly from three factors. First, there was a sharp rise in railroad employment during the war years. Increased hours of work, reten-

[8] Letter from Railroad Retirement Board, July 23, 1947.
[9] 60 Stat. 722.

tion of some employees beyond the customary retirement age, and additions to the railroad labor force, among other factors, tended to keep the tax base at a high level. The second factor is the upward trend in tax rates. For the fiscal year 1940 the average effective rate was slightly less than 2⅞ per cent for each tax—on employers and employees.[10] Moderate increases effective in later years brought the average rate for 1946 to somewhat less than 3⅜ per cent. Third, wage increases in the railroad industry have contributed to the rise in revenues.

The sharp estimated rise in the yield for 1948 over 1946 is largely a result of amendments approved in 1946, which provided for much higher rates. The rate for 1947 and 1948 was fixed at 5¾ per cent, or a combined rate of 11.5 per cent;[11] the rate formerly provided for these years was 3½ per cent, or a combined rate for the two taxes of 7 per cent. For the calendar years 1949–51 the rate will be 6 per cent for each tax, and thereafter it becomes 6¼ per cent—or a combined rate of 12.5 per cent.[12]

It follows from the above that the average rate for collections covered into the Treasury during the fiscal year 1952 will be slightly over 6 per cent for each tax, or a combined rate of over 12 per cent. The taxable railway pay roll we shall estimate at 4.5 billions, or somewhat less than that used in arriving at the revised budget estimate for 1948.[13] On this basis, railroad retirement taxes for 1952 become about 550 millions.

[10] The rate for the calendar year 1939 was 2¾ per cent, and that for the calendar year 1940 was 3 per cent. Because of the lag between the period to which the rates relate and the time when revenues are covered into the Treasury, the average rate for fiscal year 1940 collections was somewhat less than 2⅞ per cent.

[11] *Internal Revenue Code*, secs. 1500 and 1520, as amended by 60 Stat. 723–24. A corresponding increase was made in the rate for employees' representatives; sec. 1510, as amended by 60 Stat. 723.

[12] The taxable portion of the wages of railroad employees includes all amounts up to $300 per month. The maximum wages taxable in any one year thus become $3,600, as compared with $3,000 for those subject to the regular federal old-age tax.

[13] This estimate is 557 millions. Divided by the combined rate of 11.5 per cent, the tax base used becomes about 4.8 billions.

III. UNEMPLOYMENT TRUST FUND

Expenditures. Cash expenditures chargeable to the unemployment trust fund take the form of withdrawals by the states. For 1940 these withdrawals amounted to 483 millions. Thereafter there was a sharp decline to 60 millions for 1944; the comparable figure for 1945 was 70 millions. In 1946 there was a sharp increase to 1,128 millions, which was followed by a drop to 817 millions for the fiscal year 1947. The budget estimate for 1948 is 750 millions.

With no change in coverage or benefits, withdrawals in 1952 may fall in the range of 750 million to 1 billion dollars. Probable withdrawals might be 875 millions. This estimate assumes that there will be very little unemployment, perhaps only slightly more than during the fiscal year 1947.

Extension of coverage would of course mean an expansion of total requirements. However, the increase in benefits would not be proportionate at the outset, since no benefits are payable unless minimum base-period requirements as to wages have been met. For the purpose of our approximations, we shall assume that increased coverage and larger benefits will mean an increase of one fifth over the previous estimate. On this basis, the probable expenditure becomes 1,050 millions and the range 900 millions to 1,200 millions.

Taxes. The basic unemployment compensation tax is a federal tax imposed at the rate of 3 per cent.[14] However, most of the federal tax is offset by credits on account of state taxes imposed to finance unemployment compensation.[15] With

[14] *Internal Revenue Code,* sec. 1600. This tax applies only to employers of eight or more persons. The specific provision is: "The term 'employer' does not include any person unless on each of some twenty days during the taxable year, each day being in a different calendar week, the total number of individuals who were employed by him in employment for some portion of the day (whether or not at the same moment of time) was eight or more." *Internal Revenue Code*, sec. 1607 (a). Taxable wages include remuneration in a form other than cash. They do not include any amounts in excess of $3,000 per annum. Excluded employments are the same as those for the old-age taxes.

[15] In recent years the federal portion of the combined federal and state taxes has fallen in the range of 12 to 15 per cent. The 1946 federal proportion was 14.8 per cent; that for 1945 was 12.8 per cent.

a few exceptions, the original rate for the state taxes was 2.7 per cent. As merit rating became applicable or was adopted,[16] however, variable rate schedules became effective.

State revenues from unemployment compensation taxes now exceed 1 billion dollars a year. In the fiscal year 1946 the 48 states collected 1,034 millions; the comparable figure for 1945 was 1,254 millions.[17] In addition, collections by the District of Columbia were roughly 1.8 millions for 1946 and 1.6 millions for 1945.[18] Combined credits to the federal unemployment trust fund on account of deposits by the states and the District of Columbia are reported at 1,005 millions for 1947 and are officially estimated at 1,098 millions[19] for the fiscal year 1948.[20]

If coverage should be the same as in recent years, changes in the level of collections will depend on changes in the amount of taxable wages and salaries and in the average effective rate. For the period ended March 31, 1946, which corresponds roughly with that for which collections were reported during the fiscal year 1946, private wages and salaries were about 79 billions. State collections plus those of the District of Columbia were 1,036 millions for 1946, or 1.31 per cent of wages and salaries exclusive of those paid by government. We have previously placed private wages and salaries at 90 billions for 1952, or 11 billions above 1946. At an average effective

[16] At the end of 1947 only Mississippi did not have merit rating. During the year Montana, Rhode Island, Utah, and Washington put merit-rating plans into operation for the first time. *Social Security Bulletin*, Vol. 10, October 1947, p. 11.

[17] U. S. Bureau of the Census, *State Finances: 1946* (August 1946 preliminary).

[18] Computed from data in *Annual Reports of the Secretary of the Treasury on the State of the Finances*, 1944–46.

[19] Because of items unreported or in transit, these figures are not strictly comparable to the 1945 and 1946 totals above. The difference between the two bases, however, is usually very small. Another reason for the small differences is that not all state fiscal years end on June 30.

[20] We do not here discuss the revenues derived from the federal portion of the tax. These revenues are covered into the Treasury as general fund receipts, and were considered in Chap. 4. Though the amounts involved become available for general purposes, a substantial portion is in effect offset by grants to the states for administration of their unemployment compensation systems.

rate of 1.3 per cent, revenues for 1952 would thus be 1,170 millions.

Since some increase in coverage between now and 1952 is a possibility, this contingency should be taken into account in arriving at our final figure. If extensions of coverage should mean an increase of about one fifth in tax receipts, revenues would become a little over 1.4 billions.

IV. RAILROAD UNEMPLOYMENT INSURANCE ACCOUNT

Expenditures. The railroad unemployment insurance account is a separate account within the unemployment trust fund. Benefits payable through this account are estimated at 65 millions for 1952.[21] Continuation of generally favorable employment conditions in the railroad industry is assumed. Adding 5 millions for administrative expenses payable through the railroad unemployment compensation insurance administration fund, total expenditures for 1952 become 70 millions. The range is placed at 60 millions to 80 millions.

Cash receipts. Railroad companies employing eight or more persons are subject to a tax on pay rolls at a rate of 3 per cent.[22] Nine tenths of the proceeds are covered into the Treasury as trust fund receipts and credited to the railroad unemployment insurance account. The remaining one tenth is covered into the Treasury as a special account receipt and comprises the railroad unemployment insurance administration fund. Credits to this fund have been well above needs, and in recent years a substantial portion has been transferred to the railroad unemployment insurance account.[23]

Receipts for the fiscal year 1952 may amount to something like 135 millions. This figure includes the amount credited

[21] The budget estimate for 1948 is 64 millions.

[22] *Internal Revenue Code,* sec. 1600.

[23] Thus, for the fiscal year 1946 collections on account of this tax were 129 millions. Of this amount, slightly over 116 millions was credited directly to the railroad unemployment insurance account. The remaining 12.9 millions was treated as a special account receipt and credited to the railroad unemployment compensation insurance administration fund. In turn 9.6 millions of the 12.9 millions was transferred to the account.

to the administration fund. This figure was obtained by multiplying a pay-roll base of 4.5 billions by 3 per cent.

V. COMBINED CASH EXPENDITURES AND TAXES

Combined expenditures payable through the social security trust funds are estimated at 2.5 billions[24] for 1952, as indicated in the summary table on page 128. The corresponding figure for cash receipts is 4.8 billions. The indicated excess of receipts for the four funds combined is thus about 2.3 billions. The magnitude of combined receipts and expenditures, together with the excess of receipts, indicates clearly that social security finances are an important element in the over-all fiscal picture.

In earlier chapters it was assumed that in 1952 general revenues will equal expenditures. With the budget balanced on a cash basis, what disposition would be made of the 2.3 billions of excess cash receipts on social security account?[25] This sum would most likely be used to retire debt held by the public.[26] In this event, cash interest requirements would be reduced and the reserve borrowing power of the Treasury would be enhanced. On the other hand, if there should be a deficit in the regular budget roughly equal to the 2.3 billions of excess social security receipts, these funds would be used to cover the deficit. That is to say, the Treasury would be in position to meet its needs without borrowing from the public. In both cases the

[24] This figure includes small amounts for administration of railroad retirement and railroad unemployment insurance that are not payable through the trust funds. Because of numerous uncertainties, this estimate is subject to a wide margin of error.

[25] The difference here considered is significant only at the federal level. Though the unemployment compensation system for employees other than those of railroads is administered by state agencies, the transactions involved are merely of nominal significance at the state level. Collections by the states are transferred to the federal Treasury for credit to the unemployment trust fund, and the national government automatically obtains the use of any excess of receipts over requisitions for benefits.

[26] The only other possibility is that the general fund balance of the Treasury might be increased. This possibility is only of short-run significance. It is not likely that the Treasury balance would be increased indefinitely when large amounts of market debt are outstanding.

legal and accounting provisions of the several acts would of course be observed.

In concluding this discussion, it should be emphasized that the large excess of receipts here indicated should not be counted on more or less permanently. Though for some years old-age benefit payments will be less than revenues, this situation will obtain only while we are growing into the system. As the old-age system reaches maturity, the annuity payments will exceed revenues from old-age taxes by a wide margin.

CASH RECEIPTS CREDITED TO AND EXPENDITURES PAYABLE FROM SOCIAL SECURITY ACCOUNTS, ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940

(In millions of dollars)

Fund or Account	1940			1952		
	Receipts	Expenditures	Excess of Receipts	Receipts	Expenditures	Excess of Receipts
Old-age and survivors insurance trust fund	608	28	580	2,730	1,130	1,600
Railroad retirement account	121	116	5	550	245	305
Unemployment trust fund	860	483	377	1,400	1,050	350
Railroad unemployment insurance account	46	15	31	135	70	65
Combined funds..	1,635	642	993	4,815	2,495	2,320

CHAPTER VIII

TAXES IN RELATION TO NATIONAL INCOME

In this chapter taxes are compared with national income. In addition to the prospective figures for 1952, data are included for 1940 and 1946. Attention is centered on the ratio of taxes to national income; the question whether the indicated level of taxes can be supported is not considered.

Before comparing taxes with national income, we shall explain briefly what is meant by national income and why national *income* rather than gross product has been selected as a base. The national income may be defined as the returns to the people during a given year for the work they do and for the productive use of property or capital which they own. It thus includes all income payments received by the people such as wages and salaries, interest and dividends, and proprietorship incomes, together with certain forms of income accruing to them.[1] Gross national product, on the other hand, is a broader concept. It includes, in addition to the items above, all business taxes and other nontax payments to government, depreciation and depletion charges, and certain minor items.[2] Since neither business taxes nor funds derived from depreciation are available to the public, they are not a part of the money incomes of the people.

The national *income* is here used because it is out of income that virtually all taxes are paid. It comprises the fund out of which most direct taxes and indirect or shifted taxes must be met.[3] Gross national product, on the other hand, is not a suit-

[1] For example, corporate profits that are not distributed accrue only nominally to individual stockholders, but they are properly counted as a part of the national income.

[2] For a complete listing, see U. S. Department of Commerce, *Survey of Current Business,* February 1947, p. 8.

[3] Death taxes should perhaps be regarded as an exception. The income fund from which personal taxes and shifted taxes are met may actually be somewhat smaller than the national income, as traditionally defined. Such taxes cannot be paid with social security accruals or undistributed profits. However, as long as the portion of national income that is unavailable for tax payments represents only a small portion of the total, this is not especially important.

able base when the object is to consider the burden or weight of taxes. Gross national product exceeds the combined money incomes of the people by a wide margin.

The national income base used for tax comparisons should include taxes on, or measured by, business profits. If one is to compare aggregate taxes with the fund from which they are met, the portion of corporate earnings transferred directly to government should be included in the income base as well as in the tax total.[4] Moreover, inclusion of corporate income and profits taxes in the income base is essential if data for national income are to be consistently presented. Unless this is done, the contribution of corporations will not be on a basis comparable with that of other forms of business organization and professional persons.[5] The essential matter is that the net value product of incorporated and unincorporated enterprises should be accounted for in the same manner, regardless of the point at which differential profits are tapped for tax purposes.

Ratios of estimated tax collections to assumed national income for 1952, together with comparable ratios for 1940 and 1946, are shown in the table on page 131. It will be observed that the analysis is based on the *tax* totals rather than the somewhat larger *revenue* totals. In our view, the important matter is the amounts raised through the exercise of the taxing power.[6]

[4] Until recently national income data for the United States have been compiled on a basis that excluded all business taxes. The new concept of national income adopted in mid-1947, however, includes taxes on net corporate profits or income. See *National Income, Supplement to Survey of Current Business*, July 1947, pp. 11, 14.

[5] A simple illustration will suffice to make this clear. Let us suppose that a partnership which enjoys an annual net income of one million dollars decides to incorporate. The rate for the federal corporate income tax we shall assume to be 35 per cent. Under the concept of national income long used in this country, the contribution of this company to the nation's income would be automatically reduced by $350,000. Clearly, the national income cannot be reduced by the mere act of incorporation.

[6] However, one should be careful not to overemphasize the distinction between nontax revenues and taxes. Certain revenues commonly classed as taxes are closely akin to service charges; motor vehicle fuel taxes and motor vehicle licenses are familiar examples.

Our estimates suggest that in 1952 all taxes, other than social security levies, will amount to 22.1 per cent of the national income. This figure is based on combined federal, state, and local taxes of 38.6 billions and the estimate of 175 billions for national income used throughout this study. The comparable ratio for 1940 was 16.7 per cent, while that for

TAX COLLECTIONS IN RELATION TO NATIONAL INCOME, ESTIMATES FOR THE FISCAL YEAR 1952 COMPARED WITH 1940 AND 1946

I. NATIONAL INCOME AND TAX COLLECTIONS
(In billions of dollars)

Item	1940	1946	1952
National income [a]	76.0	173.0	175.0
Tax collections:			
Federal	4.8	36.8	25.4
State	3.0	4.7	5.8
Local	4.9	5.6	7.4
Total	12.7	47.1	38.6
Social security taxes	1.6	2.7	4.8
Total, including social security taxes	14.3	49.8	43.4

II. RATIO OF TAX COLLECTIONS TO NATIONAL INCOME [b]
(In percentages)

Federal	6.3	21.3	14.5
State	3.9	2.7	3.3
Local	6.5	3.2	4.3
Total	16.7	27.2	22.1
Social security taxes	2.1	1.6	2.7
Total, including social security taxes	18.8	28.8	24.8

[a] The estimate for the fiscal year 1940 was derived as follows: The 1939 and 1940 calendar year totals of the Department of Commerce were first averaged. To the figure thus obtained there was added roughly 2 billions for accruals of corporate income and profit taxes. The figure for 1946 is the average of the estimates for the calendar years 1945 and 1946; the amount added for corporate income and profits taxes was about 10 billions. The tax adjustment was necessary in order to place the 1940 and 1946 totals on a basis comparable to the postwar estimate.

[b] The ratios were computed from the rounded totals shown in this table.

1946 was 27.2 per cent. When social security taxes are included, the ratio for 1952 becomes 24.8 per cent, as compared with about 19 per cent for 1940 and roughly 29 per cent for 1946.

Federal tax collections alone for 1952 would, on the basis of our estimates, amount to a little over 14 per cent of the national income; comparable ratios for 1940 and 1946 were 6.3 per cent and 21.3 per cent. In considering these ratios, it should be kept in mind that in 1940 revenues equaled only about two thirds of expenditures; for 1952 it is assumed that revenues will be ample to cover all cash expenditures.

Our estimates indicate that in 1952 combined state and local taxes may equal about 7.6 per cent of the national income, as compared with 10.4 per cent for 1940. The indicated percentage decline is in considerable degree a result of the large increase in national income expressed in dollar terms. It is also significant that, with a national income of 175 billions, requirements for some activities such as general public assistance and unemployment relief would be sharply reduced. Stated differently, substantially full employment is not only reflected in a higher level of national income; it also influences the distribution of state and local expenditures and affects the volume of revenues required.

CHAPTER IX

CONCLUDING STATEMENT

The purpose of this study, as indicated in the preface, has been to appraise the fiscal situation—federal, state, and local—in the United States in the years before us. The method employed has been to gauge the trend of governmental expenditures, the revenue requirements, the significance of tax reduction programs, and the bearing of fluctuations in national income upon revenues.

There is a tendency in some quarters to regard the fiscal problem with easy optimism. This optimism stems largely from the fact that the federal budget currently shows a substantial surplus, even though expenditures are well above the level that had been anticipated. Moreover, the finances of most state and local governments have recently been on a sounder basis than before the war. Under the circumstances, there might seem to be little basis for concern. However, three factors raise a serious question as to our ability to maintain fiscal stability.

First, there are insistent pressures for increasing expenditures for certain purposes and against curtailment in other cases. This is evident from the fact that estimated public expenditures for 1949 are actually higher than those for the current fiscal year. Such reductions as are made tend to be more than offset by expansion elsewhere. In view of the uncertainty concerning the level of military expenditures and continuing demands for increased appropriations for other public services, the prospect for a substantial decrease in federal expenditures is, as a practical matter, not reassuring. Moreover, state and local expenditures will doubtless continue to expand.

Second, demands for tax reduction are becoming increasingly insistent. More than two years have passed since the end of hostilities, yet federal taxes (except for the excess-profits tax) are virtually on a wartime basis; and the trend in state and

local taxes is sharply upward. If all the tax-reduction proposals that have recently been advanced should be approved, revenues would be reduced by somewhere between one third and 40 per cent. Though our analysis suggests the possibility of somewhat lower rates for federal taxes, especially income taxes, the indicated level of expenditures is such that even moderate reductions in revenues might eliminate the present federal surplus.

The problem is complicated by the fact that demands for tax reduction are not effectively coupled with equally insistent demands for maximum economy in public expenditures. Compared with the specific proposals for lower taxes, demands for economy tend to be abstract and generalized in character. To the extent that such demands are diffused over the whole range —or a wide range—of expenditures, they are mainly of theoretical interest and have little effect on the volume of public expenditures.

Third, our tax structure—especially the federal tax system —is highly sensitive to changes in the economic situation. As the national income rises or falls, tax revenues tend to expand or contract more than proportionately. The "high-geared" federal tax system is especially vulnerable to reductions in national income. A moderate decline in national income could easily mean a rapid change from the present federal surplus to a deficit—even at current tax rates. Coupled with lower tax rates, a moderate decline in national income might easily mean a deficit of as much as 10 billions.

Unless the present extraordinary boom conditions continue permanently, we are certain to face serious fiscal problems. On the one hand, as we have seen, pressures continue for large governmental expenditures; on the other, demands for relief from the present burdens of taxation are increasing. It seems not improbable that both high expenditures and lower taxes may be approved, on the assumption that business activity and national income will continue at peak levels.

Perhaps the best way of describing the fiscal situation of the years immediately before us is to say that it is highly pre-

carious. Given a continued business boom, the problem of meeting the cost of government does not appear incapable of solution. However, in view of the possibility of fluctuations in national income, it remains necessary to work for the maximum reduction in expenditures consistent with the maintenance of indispensable governmental services and activities. Only thus can we expect to realize the reductions in taxes which are demanded in the interest of a healthy economy.

APPENDIX A

THE CASH BASIS AND GOVERNMENTAL BUDGETS

In this study all data for public expenditures—including the estimates for 1952—are on a cash basis. So-called expenditures that take the form of transfers to trust or other accounts which do not involve cash payments to the public have been eliminated. The use of the cash basis is essential for any analysis concerned with the broad economic aspects of governmental expenditures and revenues.

The difference between the budget basis and the cash basis is particularly important in the case of the federal government. There are several reasons why the federal budget does not clearly reflect the transactions between the government and the public.[1] First, the concept of expenditures is strictly a statutory one.[2] Certain items are classed as budget expenditures, even though no money payments are involved. Transfers to employees' retirement funds on account of the government's liability and interest earnings credited to social security and other trust funds are familiar examples. These transfers are expenditures only by definition. Unless the amounts involved are paid to the public, they have no direct economic significance; what is important is the amount of dollars paid into and paid out of the Treasury.

A second reason is that for many years only expenditures chargeable to expendable funds (general and special accounts) and the receipts credited to such funds have been included in the federal budget summaries used in deriving the official estimates of the surplus or deficit.[3] Underlying this practice is the view that trust fund expenditures and receipts have an entirely different status. From an operating budget standpoint this is correct, but it is not true in an economic sense. On the expenditure side, there is no difference what-

[1] In the President's budget for the fiscal year 1948, a document of 1,434 pages, less than two pages are devoted to a table showing "Receipts from and Payments to the Public" and the accompanying analysis.

[2] The position of the Treasury is that its task is to record and report expenditures in accordance with the requirements of law. Neither the Treasury nor the Bureau of the Budget is responsible for the disparity between "expenditures" and payments to the economy.

[3] In the budget summaries for the fiscal years 1948 and 1949, corporation accounts were also included.

ever between the economic effects of old-age payments classed as public assistance and the annuity payments from the old-age and survivors insurance trust fund. On the revenue side, the significant fact is that the cash receipts credited to this trust fund are raised through the use of the taxing power.

The disparity between the federal budget and the cash-basis federal accounts has reached large proportions. Under favorable employment conditions, a budget reported to be approximately in balance may actually mean that 3.5 billions or more of publicly-held debt is being retired or withdrawn. Similarly, a budget calling for nominal debt retirements of 2 billions might involve retirements and withdrawals of something like 5 to 6 billions.

Several questions are raised by the prospective continuing disparity between the federal budget and the cash-basis accounts. Is it realistic to formulate fiscal policy solely or primarily in terms of the regular budget? Is there any reason why a minimum debt-reduction goal of, say 2 billions a year, should be emphasized when this may mean retirements or withdrawals of market debt of several times this amount?

Our answer to the first question is that realism in federal finances requires that attention be given to the combined cash-basis accounts. Unless this is done, it is difficult to see how fiscal policy can make even a slight contribution to economic stability. Though the oft-stated goal of complete fiscal neutrality is perhaps impossible of attainment, under ordinary conditions it might be most closely approximated when payments to the public for all purposes other than debt retirement equal revenues received from the public. The official federal budget does not provide any indication when such a balance exists.

The answer to the second question is also in the negative. For the next few years, the fact that a given program of debt reduction may mean much larger retirements or withdrawals of publicly held debt might not be especially significant. In the immediate future factors other than debt retirement will doubtless be of primary importance in the determination of prices. But such a situation will not obtain permanently. For the longer-range future, any program of debt reduction related solely to the regular budget might well prove to be unworkable.

That the conventional budget does not measure the impact of governmental transactions on the economy is recognized by the President and other officials.[4] From an economic standpoint, the con-

[4] *The Economic Report of the President,* Jan. 8, 1947, p. 17; and *Midyear Economic Report of the President,* July 21, 1947, p. 24 ff.

ventional budget is misleading and the concept of a balanced budget derived therefrom is lacking in significance. Nevertheless, through tradition the legal or statutory idea of a balanced budget has become firmly imbedded and continues to be accepted as the basis for decisions of far-reaching import in the economic sphere.[5]

Until data showing payments to and receipts from the public are given a degree of prominence commensurate with their importance, the federal budget will remain unsatisfactory.[6] Orderly fiscal planning must inevitably be grounded on a careful study of the relationships between the private and governmental sectors. The significance of these observations is enhanced, when one considers that currently the goal of a balanced federal budget in the traditional sense is widely advocated.

[5] In the Ways and Means Committee and Senate Finance Committee hearings on the proposed 1947 individual income tax reduction, there were only two minor references—one by Secretary Snyder and one by Senator Taft—to a balanced budget in the economic sense. Considering the Treasury's opposition to the proposed tax reduction, it could not be expected to emphasize the cash basis. On the other hand, those favoring tax reduction apparently either regarded the traditional idea of a balanced budget as sacrosanct, or they did not view the cash basis approach as significant.

[6] In this section we do not consider the problem presented by the combined operations of all governments. The problem here considered is—at least for the present—of prime importance only at the federal level.

APPENDIX B

EXPENDITURE DATA AND ESTIMATES

In this appendix we discuss the sources of data for public expenditures used in the present study and the procedures employed in obtaining the estimates for 1952. The materials here presented should be regarded as supplementary to Chapters I and II.

The data for public expenditures in 1940 and 1946, together with other years used in preparing the estimates for 1952, have been drawn largely from official governmental sources. Perhaps the only important exception relates to federal expenditures for 1940. The 1940 figures for federal expenditures have been derived mainly from an earlier publication of the Brookings Institution.[1] The federal total for 1940 in the present study differs from that in the former publication mainly for two reasons. First, noncash items such as the transfer to the civil service retirement fund have been excluded. Second, we have included certain cash expenditures paid through trust funds.[2]

The federal figures for 1946 have been compiled mainly from the *Combined Statement of Receipts, Expenditures and Balances of the United States* for 1946. In arriving at the totals for the several functions, however, considerable use was made of data in the official federal budget and other sources. Since minor items included in the functional totals for 1946 have been estimated, no claim is made to perfect comparability with 1940.

In developing state and local data for 1940, reliance was placed mainly on the publications of the Governments Division of the United States Bureau of the Census. With a few exceptions, the 1940 data for state expenditures by functions were obtained from or based on the Bureau's publication *Financial Statistics of States: 1940.*[3] The estimates of state expenditures for 1946 have been based largely on

[1] Henry P. Seidemann, *Curtailment of Non-Defense Expenditures* (1941). The primary source of 1940 data used in preparing this study was the *Combined Statement of Receipts, Expenditures and Balances of the United States* (1940). Extensive use was also made of data and materials in the federal budget and special statements furnished by some of the departments and agencies relating to the purpose and character of expenditures.

[2] However, cash expenditures paid through the social security trust funds are considered separately. See Chap. 7.

[3] Most of the basic data for 1940 were obtained from the statistical compendium published as Vol. 3.

the Bureau's *Summary of State Government Finances in 1946*.[4]

Local data for 1940 have been based in part on a special study of the Governments Division.[5] The data in this study were especially valuable in obtaining a distribution of local expenditures by functions. Other estimates and materials which threw light on 1940 local expenditures were also examined. Since complete compilations for all units were not available, the local data for 1940 are less satisfactory than those for federal and state governments. Both the local total for 1946 and the functional distribution of local expenditures represent rough estimates. Total local costs for 1946 were estimated mainly on the basis of revenues and pay-roll costs reported by the Bureau of the Census; capital outlays were estimated at well below the 1940 level. For the functional estimates, reasonably satisfactory bases for estimating were available only for education and interest. For other functions the amounts shown for 1946 are based on scattered information and the functional distribution for 1940.

The classification of expenditures used in this study is based on the one employed in the *Curtailment of Non-Defense Expenditures* to which we have referred. The primary object of the classification there used was to show the functions or purposes of federal expenditures. Since the present study deals with all three levels of government, it was essential that the classification decided upon be usable for state and local expenditures, as well as federal expenditures. Accordingly, appropriate adjustments were made in the classification previously employed. The adaptation used in this study, it is believed, has been achieved without sacrificing any of the advantages of the classification used in the earlier analysis of federal expenditures.

The following discussion of the estimates is restricted to those functions for which it is believed supplementary data may be of value in clarifying the procedures employed.

I. NATIONAL DEFENSE

Personnel. The estimate of 9.5 billions for national defense, as stated in Chapter II, is based on an estimated military personnel of

[4] The data published in this preliminary summary release in May 1947 were supplemented by additional materials obtained through the courtesy of the Governments Division.

[5] *Financing Federal, State and Local Governments: 1941,* September 1942. Since the estimates published in this study related to 1941, appropriate adjustments were made.

1,400,000. A breakdown of this total, together with the minimum and maximum estimates, between the Army and Navy follows:

	Minimum	Maximum	Probable
Army	800,000	1,000,000	925,000
Navy	450,000	500,000	475,000
Total	1,250,000	1,500,000	1,400,000

If a compulsory military training program should be in effect, these estimates in time might be reduced to some extent. Underlying this downward adjustment are two central ideas: (1) that a compulsory training program would represent an alternative approach to national defense; and (2) that our ability to finance national defense is not unlimited. These facts are recognized by virtually all advocates of the training program, as well as by the military authorities. There is no basis for the view that the entire expense of the training program would constitute an extra cost. On the contrary, those who have explored the subject most fully have concluded that the compulsory training approach would be the least costly of the several methods of providing adequate national defense.[6]

In addition to military and naval personnel, large numbers of civilians are employed by the armed forces. The 1952 total may fall in the range of 600,000 to 750,000. Since the end of hostilities, reduction in civilian personnel has lagged behind that for military and naval personnel. It is estimated that in the fiscal year 1949 about 40 per cent of all federal civilian employees will be engaged in defense activities.

Costs. In estimating personnel costs for 1952, we have followed the procedure employed in preparing recent official budgets. That is, an independent estimate has been made for combined requirements for pay, subsistence, travel, welfare, training, clothing, and medical care. These costs have been placed at $3,000 per man; the official estimate for the fiscal year 1948 was $3,100, and the average for 1949 is placed at about $3,300. The figure of $3,000 is based on three assumptions: (1) that there will be some—perhaps an appreciable—reduction in personnel deployed overseas;[7] (2) that somewhat more economical operation will be necessary because of reduc-

[6] *A Program for National Security,* Report of the President's Advisory Commission on Universal Training, pp. 36, 93.

[7] The official estimates for 1948 were based on the assumption that roughly one half of the total personnel of the Army would be deployed overseas.

tions in appropriations; and (3) certain categories of costs might decline slightly as a result of minor downward price adjustments. Expenditures for all other military purposes have been estimated as a unit; the range for these expenditures has been placed at 5 billions to 6 billions.

II. VETERANS' BENEFITS

In 1952, as at present, the two most important components of veteran expenditures will be education and training and compensation for service-connected disabilities. However, benefits in the form of pensions and medical services, which have greater long-term significance, will be increasing.

Readjustment benefits. Education and training benefits will constitute an increasing proportion of the expenditures in this category. Unemployment allowances will terminate, in the majority of cases, on July 25, 1949.[8] The loan program will continue in full operation until July 25, 1957, and in some cases beyond that date. However, except for the contingency of default on the principal, the unit cost of loan benefits is substantially smaller than that of educational assistance. In consequence, the level of costs for readjustment benefits generally will be determined by the trend of enrollments in institutional and job training.

Although the education program will not terminate until July 25, 1956, and in some cases will continue for a longer period, the trend of enrollments during the interim will be governed by provisions with respect to the commencement of training and the duration of entitlement.[9] Over 7 million veterans have applied for certificates of eligibility and entitlement, while only 36,000 of these have exhausted their entitlement. However, about 2.1 millions have either suspended or completed their training, and another 2.8 millions are now enrolled. These figures suggest that the peak of enrollment will be established during the current year. By 1952 it will have dropped

[8] Exceptions are provided for about 1.4 million veterans who enlisted before Oct. 6, 1946, under 59 Stat. 538, but even in these cases the veterans will have only two years from the end of their enlistment during which they may claim this particular benefit.

[9] Veterans who were discharged prior to July 25, 1947 and veterans who were still in service on that date must commence their training before July 25, 1951. Veterans who enlisted under 59 Stat. 538 will have four years from the end of their enlistment in which to begin training. Some of the latter may enroll for the first time as late as 1956.

The maximum duration of entitlement is a period of four calendar years, but in individual cases the duration of entitlement is dependent on length of service. The average duration of entitlement is estimated at three calendar years or four academic years.

to a figure somewhere between 650,000 and 850,000. In view of the popularity of training benefits and the fact that many now in service are still accumulating entitlement, it is feasible to plan for the larger number.

The popularity of training would be further stimulated by the liberalization of provisions which govern the rate of expenditure for each veteran who has entitlement. The rising cost of living has focused attention particularly on allowances for subsistence.[10] Although these allowances were increased in 1945, further increases are being provided this year.[11] For some veterans they have already been approved in the form of a flat addition to allowances. For others they will result from pending revision in income ceilings.[12]

Pensions and compensation. It is obvious from the number of World War II veterans, which is now approaching 15 millions, that they will be the principal beneficiaries under this heading.[13] The principal object of expenditure during the period immediately following the war has been compensation for service-connected disability.

This class of benefit was created in connection with the changes in the veteran policy of the United States at the time of World War I. In some respects, experience with World War I veterans furnishes a guide to the trend of comparable benefits for World War II veterans. In the case of the former group, the benefit did not attain great importance until after 1923, and did not reach a peak until 1941. However, the number of active cases from World War II reached a peak of 1.7 millions in April 1947.

[10] According to a recent survey, the rate of increase in dormitory room and board is about 38 per cent since 1940–41. This figure is an average for all colleges; the average increase for public colleges is 51 per cent. *New York Times,* Sept. 23, 1947.

Tuition charges and student fees have also increased. However, the amount already authorized for tuition is more nearly commensurate with current rates.

[11] Despite evidence that Congress did not originally intend to provide for full expenses, it has responded to pressures based on the cost of living. For veterans engaged in full-time institutional training, a recent amendment provides increases ranging from $10 to $30 per month, depending on marital or dependency status. For veterans in training on the job, bills now in conference would raise the limits on the amount of subsistence which may be paid in combination with earnings.

[12] H. R. 246, 80 Cong. 2 sess. would raise these ceilings from $175 to $200 per month for veterans without a dependent; from $200 to $325 for those with one dependent; from $200 to $350 for those with more than one dependent. S. 1393 would raise the limits to $200 and $250.

[13] This is not to say that expenditures for veterans of other wars have diminished; on the contrary, they have increased.

There are two principal reasons for this earlier establishment of the load. First, there is the difference in age characteristics: World War I mobilization was largely confined to men between the ages of 20 and 30; World War II mobilization, on the other hand, ranged widely between the ages of 18 and 45.[14] The second and perhaps more significant reason is inherent in the legislative authorizations. In the case of World War II veterans, we have a more conclusive presumption of soundness at enlistment. Applications have been adjudicated solely on the basis of discharge for disability by the Army and the Navy. In many cases, the physical and mental conditions which were deemed to constitute disability from the viewpoint of the military services will have improved following return to civilian life. In consequence, a review of cases which is now in progress should result in elimination of many beneficiaries from the compensation roll.

Later, however, the number of beneficiaries will tend to increase. The main factor in this long-term trend will be the legislative status of chronic diseases, which on the basis of medical evidence cannot usually be traced conclusively to military service.[15] Historically, this problem has led to enactment by Congress of statutory presumptions of service-connection in cases diagnosed within a given period of time. In the case of World War I veterans, these statutes now cover onset or development of the disorders prior to January 1, 1925. However, in the case of World War II veterans, they cover a period of only one year after discharge from the service. If, as seems probable, the provisions which relate to World War II veterans should be liberalized by amendatory legislation, the number qualifying for disability compensation will certainly rise to a new peak.

There is also a problem with respect to the trend in unit cost, which is dependent on the average degree of disability.[16] The degrees of disability are determined by rating schedules, which are prepared by the Administrator of Veterans' Affairs. For the most part, World War I veterans are rated on the basis of a schedule

[14] The relaxation of draft standards, which is associated with a large mobilization, would inevitably result in proportionately more disabilities. Still other factors in this comparison are suggested by the duration of the conflict, and the global character of the warfare.

[15] The most important categories of such disorders are tuberculosis and the wide range of diagnostic entities which are known collectively as neuropsychiatric disease.

[16] The range is from $13.80 per month for 10 per cent disability to $138 per month for 100 per cent disability. So-called statutory compensations for specific disabilities, such as amputations or loss of sight, represent additional awards.

issued in 1925, which is more liberal than any subsequently devised. World War II veterans had previously been rated on the basis of a more economical schedule issued in 1933; however, re-ratings and new ratings in their case are now based on still another schedule issued in 1945. On the whole, the 1945 schedule is more liberal than the 1933 schedule; consequently, the average degree of disability will rise above that which has recently prevailed.

Hospital and medical care. Our estimate of costs for 1952 does not greatly exceed current requirements. Although the patient load will be substantially increased, we have assumed that the unit costs of operating the hospital and medical services can be reduced to some extent.

These services fall into two broad categories. The first is out-patient activity, which consists in part of examination for claims (pensions, compensation, need for hospital and domiciliary care, and insurance) and in part of treatments (medical and dental). The second is hospital or in-patient treatment.

The cost of medical services is mainly influenced by in-patient requirements. Out-patient treatment is confined to veterans with service-connected disabilities, while hospital treatment is authorized for all veterans, subject to the observance of certain priorities. For the increasing number of nonservice-connected disabilities, a substantially increased capacity will be provided by the current and projected construction of new hospitals, and additions to existing hospitals. Due to shortages of trained personnel, the increase in capacity available for operation will probably be slower than the increase in physical capacity.

The unit cost of medical services is perhaps more variable than that of any other type of veterans' benefit. In the case of out-patient activity, this factor has been affected by the necessity of arranging for an unusually high proportion of treatments by private physicians on a fee basis. Hospital costs have also increased drastically; the cost per patient-day has risen from $2.78 in 1941 to $8.67 in 1947. This increase is attributable in part to rising prices, but even more to the reorganization of the medical services since the war.[17] Our estimate assumes that operations may hereafter be consolidated on a basis of greater efficiency; if this is not done, expenditures would not be as moderate as here indicated.

[17] Formerly administered by nonmedical personnel, these services now operate autonomously. In 1946 Congress authorized the establishment of a Department of Medicine and Surgery, which has proceeded vigorously to improve the quality of services and recruit better qualified physicians. 59 Stat. 675.

III. REGULATION AND PROTECTION

The federal estimates under this heading are based mainly on the indicated level of expenditures for 1948, with appropriate adjustments for the growth factor. The state estimates are based largely on the expenditures for 1940, together with the trend in operating costs in more recent years. Before arriving at the estimates for local governments, pay-roll trends for city police and fire departments were examined.

IV. PROMOTION OF ECONOMIC DEVELOPMENT

Transportation. Of the federal activities in this category, reasonably satisfactory bases for estimating were available for highway grants, aids to aviation, and rivers and harbors. The estimates for these purposes are based mainly on the authorizations approved in recent years, together with the trend of expenditures since the war. The estimate for navigation aids, on the other hand, is a very rough figure. It is not possible at this time to gauge the 1952 expenditures of the Coast Guard or the Maritime Commission with any degree of accuracy.

In arriving at the estimates of state and local highway expenditures, consideration was given to: (1) projected expenditures in certain states for construction and maintenance; (2) the volume of state and local funds from user taxes, together with federal moneys becoming available; (3) the backlog of reserve funds accumulated during the war years; and (4) the possibility of continued short supplies of materials, machinery, and man power.

Other natural resources. The factors taken into account in arriving at the estimates for the Atomic Energy Commission were mentioned in Chapter II. The estimate of 450 millions is well below projected expenditures for 1949. It may be noted, however, that the expanded program has not yet been approved.

The other principal estimates under this heading were arrived at after taking into account the recent authorization measures enacted, the level of expenditures projected for 1948, and other information. As in the case of highway construction, scarcities of materials and man power may operate as limiting factors for an indefinite period.

V. PROMOTION OF SOCIAL WELFARE

Education. Federal expenditures for education other than equalization grants are based on recent expenditure data and current trends, as indicated by 1948 appropriations. The amount included for equalization grants is that carried by the Taft-Thomas-Ellender bill.

State grants to local governments for 1952 have been estimated at a figure well above the level of 1945 and 1946. Substantial increases were approved in a number of states during 1947 legislative sessions, and further increases between now and 1952 are virtually certain. Judging from recent indications, public school finance will be a major concern of many state and local governments for a number of years.

In arriving at the estimates for state educational institutions, primary attention was given to the enormous demands being placed on these institutions. The estimate for capital outlays has been influenced to some extent by the likelihood that material shortages and high costs may operate as restraining factors for something like five years.

The estimate for the operation of public day schools is the most satisfactory local estimate. Compilations of the United States Office of Education for 1945 plus the other materials referred to in Chapter II enable one to obtain a clear indication of the present level of expenditures for teachers' salaries, which account for the bulk of the total. On the other hand, expenditures for capital outlays are surrounded with no little uncertainty. Because of shortages of materials and the likelihood that the pressure of operating costs will in some cases serve to restrict new construction, the estimate for capital outlays has been placed at a moderate figure.

Public health and sanitation. The federal estimates in this category are based mainly on the expenditures indicated by existing authorizations and recent appropriations. The state and local estimates are based largely on 1940 data plus the recent trend in operating expenditures. For local governments the special financing provided by city garbage collection charges has also been taken into account.

Public assistance. Expenditures for categorical assistance have been estimated on the basis of recent trends. Federal grants to the states for the administration of unemployment compensation have been estimated on the basis of recent appropriations. In estimating public assistance payable from state and local funds, primary attention was given to recent payments.

VI. INTEREST ON PUBLIC DEBT

Federal. The estimate of 4.7 billions for federal cash interest payments, as stated in Chapter II, is based on interest-bearing debt of 215 billions. This figure does not include an estimated 40 billions of debt which will be held by trust and investment funds.

In arriving at the estimate for 1952, interest on the 215 billions has been computed at 2.2 per cent. For several years there has

been a gradual upward trend in the average interest rate. Currently, the average rate on debt held by the public is above 2 per cent.[18] The upward trend has been strongly influenced by the change in the distribution of the federal debt. From June 30, 1945 to June 30, 1947, the combined total for public issues of short- and intermediate-term obligations—Treasury notes, certificates of indebtedness, and Treasury bills—was reduced from 84.8 billions to 54.8 billions.[19] This reduction was equal to 35 per cent, as compared with about 4 per cent for all public issues. On the other hand, savings bonds which carry much higher rates have shown a steady though moderate upward trend. From June 1945 to June 1947 the amount outstanding rose from 45.6 billions to 51.4 billions.[20]

To the extent that short- and medium-term obligations are further reduced, the average rate of interest will tend to rise. However, there is little reason to believe that any decline that may occur will be at all comparable to the sharp reduction of the past two years. As long as substantial federal reserve holdings appear desirable, short-term Treasury issues are not likely to be reduced to a point where they comprise a negligible proportion of the interest-bearing debt.[21] Viewing the picture as a whole, it seems safe to assume that a further sharp reduction in short-term issues will not appreciably affect the average rate of interest on the federal debt.

State. The estimate of 145 millions for state interest payments was derived as follows: For the fiscal year 1946 the total reported as paid from general revenues was 73 millions. To this figure there was added 72 millions for interest on the estimated increase in debt. The latter figure is based on a net increase in debt of 3.6 billions and an average rate of 2 per cent.

[18] The average rate on all federal interest-bearing debt—including special issues—was 2.13 per cent on Oct. 31, 1947. However, the average rate on 29.4 billions of special issues was between 2.4 and 2.5 per cent, with the result that the average rate on public issues was very close to 2 per cent.

[19] The Treasury notes outstanding early in January 1948 carried coupon rates of 1, 1⅛, and 1½ per cent; certificates of indebtedness carried rates of ⅞, 1, and 1⅛ per cent; and Treasury bills were selling at a yield of a little less than 1 per cent.

[20] In computing the average rate of interest, Series C to E, which account for roughly 70 per cent of the total, are counted at 2.9 per cent while Series F and G are counted at 2.53 and 2.5 per cent respectively. An important reason for the upward trend in the published average rate is the increase in special issues, some of which bear interest at rates well above the average. For example, in the fiscal years 1946 and 1947 the 3 per cent notes issued to the national service life insurance fund showed an increase of 3.3 billions.

[21] On January 7, 1948, federal reserve holdings of Treasury notes, certificates of indebtedness, and Treasury bills amounted to roughly 18.6 billions. Total holdings including bonds were 21.7 billions.

Local. The estimate of 430 millions for local interest payments was derived as follows: Of the reported total of 491 millions for 1946, it was arbitrarily assumed that 104 millions was paid from the receipts of public service enterprises.[22] To the remainder of 387 millions there was added 42 millions to cover interest on the estimated increase in debt from 1946 to 1952. The latter amount would cover the interest cost on an additional indebtedness of 1.75 billions at an average rate of 2.4 per cent. The resulting total of 429 millions was arbitrarily rounded to 430 millions.

VII. GENERAL GOVERNMENT

Expenditures of the federal government have been estimated mainly on the basis of indicated expenditures for 1948. Financial administration has been increased moderately over the present level. On the other hand, the estimate for foreign relations is somewhat lower than the current level.

In estimating general government expenditures of state and local government for 1952, account was taken mainly of pay-roll costs and trends since 1940 and the growth factor. The probable influence of deferred capital construction was also considered.

[22] One half the enterprise debt times the average rate of 3.66 per cent.

INDEX